DOCKET

No. 08-674
Title: NRG Power Marketing, LLC, et al., Petitioners
v.
Maine Public Utilities Commission, et al.
Docketed: November 21, 2008
Lower Ct: United States Court of Appeals for the District of Columbia Circuit
Case Nos.: (06-1403, 06-1427, 07-1193)
Decision Date: March 28, 2008
Rehearing Denied: October 6, 2008
Questions Presented

Date	Proceedings and Orders
Nov 21 2008	Petition for a writ of certiorari filed. (Response due December 22, 2008)
Dec 17 2008	Order extending time to file response to petition to and including January 21, 2009, for all respondents .
Dec 22 2008	Brief amici curiae of Electric Power Supply Association, et al. filed.
Jan 9 2009	Order further extending time to file response to petition to and including February 20, 2009, for all respondents.
Feb 13 2009	Order further extending time to file response to petition to and including March 18, 2009, for all respondents.
Mar 18 2009	Brief of respondent Federal Energy Regulatory Commission filed.
Mar 18 2009	Brief of respondent Richard Blumenthal, et al.
Mar 18 2009	Brief amici curiae of American Public Power Association, et al. filed.
Apr 1 2009	DISTRIBUTED for Conference of April 17, 2009.
Apr 1 2009	Reply of petitioners NRG Power Marketing, LLC, et al. filed. (Distributed)
Apr 20 2009	DISTRIBUTED for Conference of April 24, 2009.
Apr 27 2009	Petition GRANTED.
May 28 2009	The time within which to file the joint appendix and petitioners' brief on the merits is extended to and including July 7, 2009.
May 28 2009	The time within which to file respondents' briefs on the merits is extended to and including September 4, 2009.
Jul 7 2009	Brief of respondent Federal Energy Regulatory Commission in support of petitioners filed.
Jul 7 2009	Brief of petitioners NRG Power Marketing, LLC, et al. filed.
Jul 7 2009	Joint appendix filed. (Statement of costs received).
Jul 10 2009	Consent to the filing of amicus briefs, in support of either party or of neither party, received from counsel for the petitioners.
Jul 10 2009	Consent to the filing of amicus briefs, in support of either party or of neither party, received from counsel for the respondents.
Jul 14 2009	Brief amici curiae of Morgan Stanley Capital Group Inc., et al. filed.
Jul 14 2009	Brief amici curiae of Colin C. Blaydon, et al. filed.
Jul 14 2009	Brief amici curiae of Electric Power Supply Association, et al. filed.
Aug 17 2009	SET FOR ARGUMENT ON Tuesday, November 3, 2009.
Aug 17 2009	CIRCULATED.

Aug 21 2009	Record received from U.D.C.A. for DC Circuit. (1 box)
Sep 4 2009	Brief of respondent Maine Public Utilities Commission, et al. filed. (Distributed)
Sep 10 2009	Motion for divided argument filed by respondent Federal Energy Regulatory Commission in support of petitioners.
Sep 11 2009	Brief amici curiae of Public Citizen, Inc., et al. filed. (Distributed)
Sep 11 2009	Brief amicus curiae of Public Utilities Commission of the State of California filed. (Distributed)
Sep 11 2009	Brief amici curiae of American Public Power Association, et al. filed. (Distributed)
Sep 25 2009	Record received from FERC. (15 boxes. There is 1 CD included in this record)
Oct 5 2009	Motion for divided argument filed by respondent Federal Energy Regulatory Commission in support of petitioners GRANTED.
Oct 5 2009	Reply of respondent Federal Energy Regulatory Commission in support of petitioners filed. (Distributed)
Oct 5 2009	Reply of petitioners NRG Power Marketing, LLC, et al. filed. (Distributed)
Nov 3 2009	Argued. For petitioners NRG Power Marketing, LLC, et al.: Jeffrey A. Lamken, Washington, D.C. For respondent FERC in support of petitioners: Eric D. Miller, Assistant to the Solicitor General, Department of Justice, Washington, D.C. For respondents: Gen. Richard Blumenthal, Hartford, Conn.

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PETITION FOR WRIT OF CERTIORARI

Supreme Court, U.S.
FILED
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No. 08-674

IN THE
Supreme Court of the United States

NRG POWER MARKETING, LLC, *ET AL.*,
Petitioners,
v.
MAINE PUBLIC UTILITIES COMMISSION, *ET AL.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Section 206 of the Federal Power Act (FPA), 16 U.S.C. § 824e(a), requires that rates for the transmission and sale of electricity in interstate commerce be "just and reasonable." Under the *Mobile-Sierra* doctrine—named for this Court's decisions in *United Gas Pipeline Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956), and *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956)—the Federal Energy Regulatory Commission ("FERC") must "presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law," and that "presumption may be overcome only if FERC concludes that the contract seriously harms the public interest." *Morgan Stanley Capital Group Inc.* v. *Pub. Util. Dist. No. 1*, 128 S. Ct. 2733, 2737 (2008). In the decision below, the court of appeals held that, "when a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply." The question presented is:

Whether *Mobile-Sierra*'s public-interest standard applies when a contract rate is challenged by an entity that was not a party to the contract.

PARTIES TO THE PROCEEDINGS BELOW

Petitioners NRG Power Marketing, LLC (formerly NRG Power Marketing, Inc.), Devon Power LLC, Connecticut Jet Power LLC, Norwalk Power LLC, Middletown Power LLC, Montville Power LLC, and Somerset Power LLC intervened in the court of appeals and were parties in proceedings before the Federal Energy Regulatory Commission.

The following parties before the Federal Energy Regulatory Commission also intervened for the respondent in the court of appeals: Connecticut Department of Public Utility Control; TransCanada Power Marketing, Ltd.; International Power America, Inc.; Bridgeport Energy, LLC; Casco Bay Energy Co., LLC; NEPOOL Participants Committee; Milford Power Co., LLC; FPL Energy, LLC; Entergy Nuclear Generation Co., LLC; Entergy Nuclear Vermont Yankee, LLC; Mirant Energy Trading, LLC; Mirant Kendall, LLC; Mirant Canal, LLC; Boston Generation, LLC; Mystic I, LLC; Mystic Development, LLC; Fore River Development, LLC; Massachusetts Municipal Wholesale Electric Co.; Connecticut Municipal Electric Energy Cooperative; ISO New England, Inc.; Lake Road Generating Co.; Berkshire Power Co., LLC; MASSPOWER; Dominion Resources, Inc.; Dominion Energy Marketing, Inc.; Dominion Nuclear Connecticut, Inc.; Central Vermont Public Service Co.; PSEG Power, LLC; and PSEG Energy Resources & Trade LLC.

The Federal Energy Regulatory Commission was respondent in the court of appeals and is therefore a respondent here under this Court's Rule 12.6.

Respondents Maine Public Utilities Commission, the Attorney General of Massachusetts, and the Attorney General of Connecticut were the petitioners in the court

of appeals and parties before the Federal Energy Regulatory Commission.

The following parties before the Federal Energy Regulatory Commission intervened for the petitioners in the court of appeals: Industrial Energy Consumer Group; NEPOOL Industrial Customer Coalition; and NSTAR Electric & Gas Corp.

CORPORATE DISCLOSURE STATEMENT

Pursuant to this Court's Rule 29.6, petitioners NRG Power Marketing, LLC, Devon Power LLC, Connecticut Jet Power LLC, Norwalk Power LLC, Middletown Power LLC, Montville Power LLC, and Somerset Power LLC state that they are subsidiaries of NRG Energy, Inc. and that they have no outstanding shares of stock owned by the public. NRG Energy, Inc. is a Delaware corporation whose common stock is held by the public. NRG Energy, Inc. has no parent company and no publicly held company has a 10 percent or greater ownership in NRG Energy, Inc.

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IN THE

Supreme Court of the United States

NRG POWER MARKETING, LLC, *ET AL.*,
Petitioners,

v.

MAINE PUBLIC UTILITIES COMMISSION, *ET AL.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

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PETITION FOR A WRIT OF CERTIORARI

NRG Power Marketing, LLC, Devon Power LLC, Connecticut Jet Power LLC, Norwalk Power LLC, Middletown Power LLC, Montville Power LLC, and Somerset Power LLC respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the District of Columbia Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-27a) is reported at 520 F.3d 464. The order of the Federal Energy Regulatory Commission (Pet. App. 102a-223a) is reported at 115 FERC ¶61,340, and the order on rehearing (Pet. App. 28a-101a) is reported at 117 FERC ¶61,133.

JURISDICTION

The court of appeals entered its judgment on March 28, 2008. The court denied rehearing and rehearing en

banc on October 6, 2008. Pet. App. 241a-248a. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

Relevant provisions of the Federal Power Act, tit. II, ch. 687, 49 Stat. 803, 838-63 (codified as amended at 16 U.S.C. §§ 824-824w), are set forth at Pet. App. 251a-261a.

STATEMENT OF THE CASE

I. STATUTORY FRAMEWORK

A. The Federal Power Act

The Federal Power Act ("FPA"), 16 U.S.C. § 824 *et seq.*, gives the Federal Energy Regulatory Commission ("FERC") "exclusive authority to regulate the transmission and sale at wholesale of electric energy in interstate commerce." *New England Power Co.* v. *New Hampshire*, 455 U.S. 331, 340 (1982); see 16 U.S.C. § 824. Section 205 of the Act requires that "[a]ll rates * * * made, demanded, or received" by wholesale sellers of electricity be "just and reasonable," 16 U.S.C. § 824d(a), and bars discriminatory pricing, *id.* § 824d(b). Under FPA § 205, sellers must file "schedules showing all rates and charges * * * together with all contracts" for the sale of wholesale electricity in interstate commerce. *Id.* § 824d(c). Sellers must also notify FERC of proposed rate changes. See *id.* § 824d(d).

Section 206 defines FERC's authority to change rates. Under that provision, FERC can investigate the lawfulness of any rate on its own motion or on complaint. 16 U.S.C. § 824e(a). If FERC finds a rate "unjust, unreasonable, unduly discriminatory or preferential," it must "determine the just and reasonable rate * * * to be thereafter observed and * * * shall fix the same by order." *Ibid.* FERC may order refunds of unjust or unreasonable charges made after the investigation or complaint is initiated. See *id.* § 824e(b).

The FPA "'departed from the [traditional] scheme of purely tariff-based regulation'" by allowing parties to

negotiate contract rates. *Morgan Stanley Capital Group Inc.* v. *Pub. Util. Dist. No. 1*, 128 S. Ct. 2733, 2738, 2747 (2008) (quoting *Verizon Commc'ns Inc.* v. *FCC*, 535 U.S. 467, 479 (2002)). The FPA recognizes that parties to wholesale power contracts are generally "sophisticated businesses enjoying presumptively equal bargaining power, who could be expected to negotiate a 'just and reasonable' rate as between the two of them." *Verizon*, 535 U.S. at 479. "The regulatory system created by the Act" thus "is premised" on preserving "contractual agreements voluntarily devised by the regulated companies." *Permian Basin Area Rate Cases*, 390 U.S. 747, 822 (1968).[1]

B. The *Mobile-Sierra* Doctrine

The *Mobile-Sierra* doctrine at issue here arises from this Court's twin decisions in *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956) ("*Mobile*"), and *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956) ("*Sierra*"). *Mobile-Sierra* limits FERC's authority under FPA §206 to authorize or require changes in rates set by contract. See *Morgan Stanley*, 128 S. Ct. at 2738-40. In both *Mobile* and *Sierra*, sellers filed rate schedules and contracts with FERC's predecessor, the Federal Power Commission. *United Gas Pipe Line Co.*, 5 FPC 770 (1946); *Pac. Gas & Elec. Co.*, 7 FPC 832 (1948).

In *Mobile*, the seller unilaterally filed a new rate to replace an unfavorable contract rate. The Court declared that unilateral attempts to abrogate a previously-filed contract, by submitting a new rate for review, are a "nullity." 350 U.S. at 339. The Court held that, even if the new rate would be just and reasonable, an existing

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[1] For many years, such contracts or rate formulas were filed with FERC, although FERC has since shifted to a market-based system that does not require each contract be filed before becoming effective. *Morgan Stanley*, 128 S. Ct. at 2740-42.

rate set by agreement between the parties may not be set aside unless it "conflict[s] with the public interest." *Id.* at 345.[2]

In *Sierra*, the Court held that the public-interest standard applies *even if* the Commission finds that the prior contract rate would be unjust and unreasonable absent an existing agreement. See 350 U.S. at 353-54. When a rate is established by contract, FERC's authority is limited: "[A] contract may not be said to be either 'unjust' or 'unreasonable' simply because it is unprofitable to the public utility." *Id.* at 355. Instead, a contract rate may be abrogated as contrary to the "public interest" only if it "might impair the financial ability of a public utility to continue its service, cast upon other consumers an excessive burden, or be unduly discriminatory." *Ibid.* Because "[t]he regulatory system created by the Act is premised on contractual agreements voluntarily devised by the regulated companies[,] it contemplates abrogation of these agreements only in circumstances of unequivocal public necessity." *Permian Basin*, 390 U.S. at 822.

That protection for contractually negotiated rates, the Court explained, is critical not merely to the contracting parties but also to the welfare of the markets. Energy infrastructure projects, particularly power generation projects, are enormously capital intensive and may take years to complete; absent assurances that agreements to purchase electricity at a specific rate will be enforced, few could risk making those investments. "By preserving the integrity of contracts," the *Mobile-Sierra* doctrine "permits the stability of supply arrangements which

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[2] While *Mobile* arose under the Natural Gas Act, key sections of that Act and the FPA are "substantially identical," 350 U.S. at 353, and the Court has "cite[d] interchangeably decisions interpreting the pertinent sections of the two statutes," *Ark. La. Gas Co.* v. *Hall*, 453 U.S. 571, 577 n.7 (1981).

all agree is essential to the health of the * * * industry." *Mobile*, 350 U.S. at 344. "[U]ncertainties regarding rate and contract sanctity can have a chilling effect on investments and a seller's willingness to enter into long-term contracts and this, in turn, can harm consumers in the long run." *Morgan Stanley*, 128 S. Ct. at 2749 (quoting 72 Fed. Reg. 39,904, 39,906-907). Power markets "cannot attract the capital needed to build adequate generating infrastructure" unless everyone understands that FERC will uphold contract rates absent "*extraordinary* circumstances." *Nev. Power Co.* v. *Duke Energy Trading & Mktg., L.L.C.*, 99 FERC ¶61,047, 61,190 (2002).

This Court has also held that contracting parties can agree that a different standard—not the *Mobile-Sierra* public-interest standard—should govern future modifications. See *United Gas Pipe Line Co.* v. *Memphis Light, Gas & Water Div.*, 358 U.S. 103, 110-13 (1958) ("*Memphis*"). Such provisions are known as "*Memphis* clauses." But, absent such a clause, *Mobile-Sierra* requires FERC to "presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law." *Morgan Stanley*, 128 S. Ct. at 2737. That "presumption" applies once the contract is signed "regardless of when the contract is reviewed," and it "may be overcome only if FERC concludes that the contract seriously harms the public interest." *Id.* at 2737, 2745-46.

II. Proceedings Below

A. The New England Capacity Market

This case arises out of FERC's efforts to ensure the reliability of the electric power system in New England. To maintain reliability, regulators and utilities must ensure that the electric system has sufficient generation capacity to respond to peak demand. System operators measure the adequacy of generation by "installed capa-

city"—the volume of electricity each power plant can produce.

More than three decades ago, the electric system operators in New England "pooled" their systems to form the "New England Power Pool." See *NEPOOL Power Pool Agreement*, 48 FPC 538, 549 (1972). In the late 1990s, the New England electric markets again restructured, turning over operation of the transmission system to an "Independent System Operator[]," an entity charged with "operat[ing] transmission facilities in a nondiscriminatory manner." *Morgan Stanley*, 128 S. Ct. at 2741. Dubbed "ISO-NE," that new entity began administering auction-based markets for electricity. This case arises from further reforms to that market.

B. Proceedings Before FERC

1. The Proceedings And Settlement

The ISO-NE capacity market failed to function as anticipated. "For many years" it was "rife with problems." Pet. App. 2a. The market did not provide sufficient incentives to retain or attract generation capacity. "As the Commission explained in 2003, 'existing generators needed for reliability are not earning sufficient revenues (and are in fact losing money), and [] additional infrastructure is needed soon to avoid violations of reliability criteria.'" *Ibid.* (quoting Pet. App. 137a). "In other words, the supply of capacity was barely sufficient to meet the region's demand." *Ibid.*

To resolve those problems, FERC ordered ISO-NE to revise its capacity market to compensate existing generators and promote construction of new generation where needed to maintain grid reliability. *Devon Power LLC*, 103 FERC ¶61,082 at 61,271 (2003). ISO-NE complied by filing a new locational installed capacity market mechanism, which FERC then set for hearing under FPA §206. *Devon Power LLC*, 107 FERC ¶61,240 at 62,020 (2004). Years of litigation ensued. Eventually,

all but eight of the 115 participants reached a settlement. Pet. App. 5a. Among the opponents were the Maine Public Utilities Commission and the Attorneys General of Connecticut and Massachusetts. Only one wholesale customer in the market opposed the agreement.

The new agreement created a "forward" capacity market. Under that new approach, ISO-NE would run an annual auction, and the winning suppliers (those with the lowest prices) would be obligated to provide capacity for a one-to-five year period starting three years in the future. Pet. App. 110a-111a. That design would "allow potential new capacity to compete in the auctions" by letting new entrants bid based on their willingness to build additional generating plants. *Ibid.* If a new generator were chosen at auction, it would be obligated to construct its new plant within three years, and it would receive fixed payments for up to five years to support necessary capital investment and financing. *Id.* at 110a-111a, 113a. The new market structure did not, however, compensate existing suppliers of capacity until the end of the three-year lead-time period. To bridge that gap, the settlement also included transition payments to existing suppliers to compensate them for continuing to make their capacity available. *Id.* at 116a-118a.

2. This petition concerns disagreement over the standard that would govern *future* challenges to the amount of the transition payments or the rates agreed upon as a result of the auction process; it does not concern the standard FERC applied in this case when deciding whether to approve the settlement agreement itself. With respect to such potential future challenges, the agreement included a *Memphis* clause that generally exempted any such challenges from operation of the *Mobile-Sierra* presumption of reasonableness. Pet. App. 193a-194a (quoting agreement § 4C). But the *Memphis* clause excepted two items: (1) the transition payments to

existing generators; and (2) the requirement that winning bidders in the capacity market be paid the amount set at auction. *Ibid.* The agreement specified that, with respect to those items, the *Mobile-Sierra* standard would apply to all future challenges, "whether the change is proposed by a Settling Party, a non-Settling Party, or the FERC acting *sua sponte*." *Ibid.* The parties explained that, for transition capacity and future capacity markets, stability and certainty were absolutely critical, both to ensure that existing generators would continue to supply necessary capacity, and to provide the incentive for new entrants to invest the large sums necessary to build additional capacity. See *id.* at 196a-197a.

Consistent with FERC's regulations and precedent regarding contested settlements, the agreement provided that FERC would review the agreement itself (including the transition payments, auction, and review provisions) under the ordinary just-and-reasonable standard. 18 C.F.R. §385.602(h); *Trailblazer Pipeline Co.*, 85 FERC ¶61,345 at 62,339-45 (1998), order on reh'g, 87 FERC ¶61,110 at 61,438 (1999). But, once FERC found the agreement just and reasonable and any judicial review was complete, future challenges to auction prices or transition payments (whether based on changed circumstances or otherwise) would be governed by *Mobile-Sierra*. After each auction, ISO-NE would file the resulting auction price with FERC under FPA §205. Because the auction price reflected a voluntary agreement between a willing buyer and willing seller, anyone later challenging the auction price would have to overcome the *Mobile-Sierra* presumption. Likewise, once FERC accepted the transition payment schedule, any new challenge to those rates would be governed by *Mobile-Sierra* as well.

2. FERC's Decision

FERC approved the agreement as "a just and reasonable outcome for this proceeding consistent with the public interest." Pet. App. 103a. It specifically addressed section 4C's requirement that future challenges to transition payments (provided in the agreement) or to future auction prices (once mutually agreed-upon through the auction and filed with FERC) would be subject to *Mobile-Sierra* public-interest review. *Id.* at 200a-203a. FERC rejected the claim that *Mobile-Sierra* could not apply to future challenges brought by third parties. *Id.* at 194a, 196a. FERC explained that it had "routinely permitted the use of similar provisions in settlement agreements, including contested settlements." *Id.* at 200a & n.150 (listing cases). And FERC reaffirmed the validity of such provisions, declaring that there is "no Commission or court precedent that supports a finding that a non-signatory may unilaterally seek changes to a *Mobile-Sierra* 'public interest' contract under the 'just and reasonable' standard of review." *Id.* at 200a-201a (quoting *Pennsylvania-New Jersey-Maryland Interconnection*, 108 FERC ¶61,032 at 61,204 (2004) (citing *Pub. Utils. Comm'n of Cal.*, 105 FERC ¶61,182 at 61,947 (2003))).

FERC also found that applying *Mobile-Sierra* review to third-party rate challenges does not deny third parties any rights. "'[T]he *Mobile-Sierra* doctrine itself allows for intervention by FERC where it is shown that the interests of third parties are threatened,'" because the Supreme Court's *Mobile-Sierra* test specifically requires FERC to protect outside parties from "'undue discrimination' or imposition of an 'excessive burden.'" Pet. App. 201a & n.153 (quoting *Ne. Utils. Serv. Co.* v. *FERC*, 993 F.2d 937, 961 (1st Cir. 1993)) (citing *Papago Tribal Util. Auth.* v. *FERC*, 723 F.2d 950, 953 n.4 (D.C. Cir. 1983) (recognizing FERC's ability under *Mobile-Sierra* to re-

dress contract rates that are "unduly discriminatory or preferential to the detriment of purchasers who are not parties to the contract")). Commissioner Kelly concurred, emphasizing that the agreement used the "*Mobile-Sierra* public interest standard in a very constrained and time-limited manner," applying it "only to the stated transition period prices and the annual prices generated each year by the [capacity market] auctions." Pet. App. 223a. FERC later denied rehearing. Pet App. 75a-79a.

C. Proceedings In The D.C. Circuit

1. The Panel Decision

The D.C. Circuit granted the petition for review in relevant part but denied it in all other respects. Pet. App. 1a-27a.[3] Before the D.C. Circuit, some parties again urged that *Mobile-Sierra*'s presumption of reasonableness could not be applied to future challenges filed by those who were not parties to the agreement. Applying that presumption, they urged, would "deprive them of their statutory right to challenge rates under the 'just and reasonable' standard." *Id.* at App. 19a. Unlike FERC, the court of appeals regarded the scope of *Mobile-Sierra*'s application to non-contracting objectors as a question of first impression.

The panel agreed that, under the *Mobile-Sierra* doctrine, "'FERC may abrogate or modify freely negotiated private contracts that set firm rates or establish a specific methodology for setting the rates for service . . . only if required by the public interest.'" Pet. App. 19a. (quoting *Atl. City Elec. Co.* v. *FERC*, 295 F.3d 1, 14 (D.C. Cir. 2002)). Under that standard, contract rates or methodologies cannot be altered except "for the most

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[3] The portions of the D.C. Circuit's decision upholding FERC's decision, including FERC's ruling that the transition payments and the auction mechanism were just and reasonable, Pet. App. 8a-11a; see also *id.* at 11a-19a, 24a-26a (upholding other FERC determinations), are not challenged or at issue in this petition.

compelling reasons," such as where they would "'impair the financial ability of the public utility to continue its service, cast upon other customers an excessive burden, or be unduly discriminatory.'" *Id.* at 20a-21a (quoting *Sierra*, 350 U.S. at 355).

But the panel also observed that, under FPA § 206, "when a party files a complaint against a rate or charge, FERC must adjudicate the challenge under the 'just and reasonable' standard." Pet. App. 20a. The panel then characterized *Mobile-Sierra*'s public-interest test as having "carv[ed] out an exception to this rule based on the 'familiar dictates of contract law.'" *Ibid.* (quoting *Borough of Lansdale* v. *FPC*, 494 F.2d 1104, 1113 (D.C. Cir. 1974)). The exclusive purpose of *Mobile-Sierra*, in the panel's view, was "to ensure contract stability *as between the contracting parties*." Pet. App. 24a (quoting *Atl. City*, 295 F.3d at 14).

The panel therefore held that *Mobile-Sierra* applies only "when '*one party to a rate contract* on file with FERC attempts to effect a unilateral rate change,'" and is inapplicable when a *non-party* attempts to alter the rates. Pet. App. 22a (quoting *Me. Pub. Utils. Comm'n* v. *FERC*, 454 F.3d 278, 284 (D.C. Cir. 2006)) (emphasis added). A contract, the panel asserted, "cannot bind a nonparty." *Ibid.* (quoting *EEOC* v. *Waffle House, Inc.*, 534 U.S. 279, 294 (2002)). "[W]hen a rate challenge is brought by a non-contracting third party," the panel summarized, "the *Mobile-Sierra* doctrine simply does not apply; the proper standard of review remains the 'just and reasonable' standard in section 206 of the Federal Power Act." *Ibid.* A contrary holding, the court stated, would "deprive[] non-settling parties of their statutory right" to have future "rate challenges adjudicated under the" statutory "'just and reasonable standard' * * * in cases of changed circumstances." *Id.* at 22a-23a.

The panel did not dispute that FERC had long applied *Mobile-Sierra* to third-party challenges. Pet. App. 23a. That longstanding position, the court stated, "does not necessarily support the policy's legality, since none of the cited orders have been subject to judicial review on the *Mobile-Sierra* issue." *Ibid.* And the court rejected FERC's contention that *Mobile-Sierra* was necessary "to promote price certainty and contract stability"—features that are indispensable to promoting investment in the large and long-term infrastructure projects required in the energy sector. *Id.* at 24a. Instead, the court reiterated its view that *Mobile-Sierra* provides contract stability only between the contracting parties, and does not apply to those who are not parties to the agreement. *Ibid.*

2. This Court's Decision In Morgan Stanley *And The Rehearing Petitions*

After the court of appeals issued its decision, this Court issued its decision in *Morgan Stanley*. In that case, this Court rejected the claim that the *Mobile-Sierra* public-interest standard is an atextual "exception" to the statutory "just and reasonable" standard. Reaffirming *Mobile-Sierra* and reversing a Ninth Circuit decision that declined to apply the doctrine in instances of alleged market failure, this Court rejected as "indefensible" the claim that *Mobile-Sierra* represents a departure from the statutory "just and reasonable" standard in FPA § 206. 128 S. Ct. at 2740. The Court explained that, while "[t]here is only one statutory standard," *id.* at 2745, the *Mobile-Sierra* public-interest standard is a "differing *application* of that just-and-reasonable standard to contract rates." *Id.* at 2740. *Mobile-Sierra* requires FERC to "presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law." *Id.* at 2737. And that mandatory "presumption may be overcome only

if FERC concludes that the contract seriously harms the public interest." *Ibid.*

Relying on *Morgan Stanley*, FERC and petitioners urged (among other things) that the panel had erred by characterizing *Mobile-Sierra* as an "exception" to the just-and-reasonable standard, Pet. App. 20a, and thus in "agree[ing]" that any application of that standard to challenges by non-parties would "deprive them of their statutory right to challenge rates under the 'just and reasonable' standard," *id.* at 19a. Under *Morgan Stanley*, they explained, the *Mobile-Sierra* public-interest standard is merely an "application" of the just-and-reasonable standard to contract rates. See FERC C.A. Reh'g Pet. 3-4, 6.[4]

On August 22, 2008, the court of appeals ordered a response to the rehearing requests. Pet. App. 249a-250a. On October 6, 2008, the court of appeals denied the petitions for rehearing and rehearing en banc. *Id.* at 241a-248a.

REASONS FOR GRANTING THE PETITION

For 50 years, the *Mobile-Sierra* presumption has encouraged investment in energy infrastructure by protecting contract rates. Under that doctrine, FERC must "presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law." *Morgan Stanley Capital Group Inc.* v. *Pub. Util. Dist. No. 1*, 128 S. Ct.

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[4] Two FERC Commissioners dissented from the decision to seek rehearing. Pet. App. 224a. They indicated that a contested settlement itself should not be reviewed under the *Mobile-Sierra* standard, *id.* at 228a-229a (a position that was wholly consistent with the fact that FERC reviewed the settlement in this case under the ordinary just-and-reasonable standard, *id.* at 234a). This petition, however, concerns whether *Mobile Sierra* can apply when non-parties bring *future* challenges to, for example, the rate set between a willing buyer and a willing seller in the forward capacity auctions—rates that generators must rely on to build new power plants over lengthy periods.

2733, 2737 (2008). That "presumption may be overcome only if FERC concludes that the contract seriously harms the public interest." *Ibid.* *Mobile-Sierra*'s public-interest standard precludes FERC from modifying or abrogating contract rates except in the most compelling cases. "[S]etting aside a contract rate requires a finding of 'unequivocal public necessity,' *Permian Basin [Area Rate Cases]*, 390 U.S. [47,] 822 [(1968)], or 'extraordinary circumstances,' *Arkansas Louisiana Gas Co.* v. *Hall*, 453 U.S. 571, 582 (1981)." *Morgan Stanley*, 128 S. Ct. at 2748.

Time and again this Court and FERC have recognized that *Mobile-Sierra* is critical to electricity and natural gas markets. "By preserving the integrity of contracts," *Mobile-Sierra* "permits the stability of supply arrangements which all agree is essential to the health of the * * * industry." *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332, 344 (1956). "[U]ncertainties regarding rate and contract sanctity can have a chilling effect on investments." *Morgan Stanley*, 128 S. Ct. at 2747 (quoting 72 Fed. Reg. 39,904, 39,906-907). "Competitive power markets simply cannot attract the capital needed to build adequate generating infrastructure without regulatory certainty, including certainty that the Commission will not modify market-based contracts unless there are *extraordinary* circumstances." *Nev. Power Co.* v. *Duke Energy Trading & Mktg., L.L.C.*, 99 FERC ¶61,047, 61,190 (2002). Just last Term, this Court reaffirmed that the *Mobile-Sierra* doctrine is a "key source of stability" that reduces "volatility in[] the electricity markets" and thus "ultimately benefits consumers." 128 S. Ct. at 2749.

The decision below nonetheless holds that the *Mobile-Sierra* doctrine "simply does not apply" to the efforts of *non-parties* to challenge a contract rate. Pet. App. 22a. That unprecedented holding destroys the certainty and

stability that the electricity and natural gas markets require and that *Mobile-Sierra* attempts to provide. *Mobile-Sierra* cannot provide contractual certainty or stability if it applies *only* to challenges by contracting parties, but allows contract modification under a less rigorous standard in challenges brought by *anyone* else—whether it be one of millions of ratepayers, a state representative, a state attorney general (*parens patriae*), or FERC itself.

That destabilization will have a profound impact on the industry's ability to invest the enormous capital required to build additional power plants, transmission lines, and pipelines necessary to meet the demands of already energy-starved markets. This Court's decision in *Morgan Stanley* last Term rejected the Ninth Circuit's efforts to marginalize *Mobile-Sierra* as a species of "estoppel doctrine." 128 S. Ct. at 2746. This Court should likewise reject the current effort to marginalize *Mobile-Sierra* by making it applicable only when the challenge is brought by a contractual counterparty—but not when the challenge is brought by any one of the millions of other possible complainants.

The decision below, moreover, reaches that result by invoking a construction of the FPA indistinguishable from the one this Court rejected in *Morgan Stanley*. The D.C. Circuit ruled that the *Mobile-Sierra* "public-interest" test is "an exception" to the statutory just-and-reasonable standard in FPA § 206, 16 U.S.C. § 824e(a), and that applying it would deny third parties "their statutory right to challenge rates under the 'just and reasonable' standard." Pet. App. 19a, 20a; accord *id.* at 22a ("[W]hen a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply; the proper standard of review remains the 'just and reasonable' standard in [FPA § 206]."). But this Court's decision in *Morgan Stanley* rejected, as

"obviously indefensible," the proposition that the *Mobile-Sierra* public-interest standard is "different from the statutory just-and-reasonable standard." 128 S. Ct. at 2740. Instead, the Court explained, the public-interest test represents a "differing *application* of that [statutory] just-and-reasonable standard to contract rates." *Ibid.* The decision below thus does not merely eviscerate a critical, 50-year-old protection against abrogation or modification of contract rates. It does so using a theory this Court just rejected last Term. Given the decision's dramatic consequences for electricity and gas markets, this Court's review is both warranted and necessary.

I. The Decision Below Raises An Issue Of Exceptional Importance And Upsets Decades Of Settled Understanding

The *Mobile-Sierra* doctrine has, for half a century, played a critical role in the development and preservation of our Nation's energy infrastructure. The decision below threatens to turn that doctrine into a legal relic that applies only when rate challenges are brought by the direct counterparties in a contract. That ruling overturns decades of settled understanding and eliminates the stability and certainty that are critical to the maintenance and development of energy infrastructure.

A. *Mobile-Sierra* Has Been Critical To The Development Of Energy Infrastructure For Decades

This Court's twin decisions in *Mobile*, *supra*, and *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956) ("*Sierra*"), establish what is now a bedrock principle of energy law: When two parties establish a wholesale rate by contract, FERC may not upset that rate unless it "conflict[s] with the public interest." *Mobile*, 350 U.S. at 345. That "public-interest" test is more demanding than the ordinary "just-and-reasonable" standard that FERC employs where the parties have not reached agreement. Absent a contract, FERC may reject a rate as "unjust"

or "unreasonable" if, for example, it would be unprofitable to one party. But once the parties agree to a rate by contract, that rate "may not be said to be either 'unjust' or 'unreasonable' simply because it is unprofitable to the public utility." *Sierra*, 350 U.S. at 355. Instead, a contract rate may be abrogated as contrary to the "public interest" only if it "might impair the financial ability of the public utility to continue its service, cast upon other consumers an excessive burden, or be unduly discriminatory." *Ibid.* Because "[t]he regulatory system created by the Act is premised on contractual agreements voluntarily devised by the regulated companies[,] it contemplates abrogation of these agreements only in circumstances of unequivocal public necessity." *Permian Basin*, 390 U.S. at 822.

That doctrine is critical to energy providers and consumers alike. Building the infrastructure to generate and transmit electricity and natural gas requires enormous capital investments over lengthy periods. Absent certainty that promised rates will be paid, the incentive to build necessary infrastructure evaporates.[5] And because energy markets are exceedingly volatile, long-term fixed-price contracts are an essential hedge against volatility.[6] For those reasons, this Court's pathmarking

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[5] See Lawrence J. Makovich, *California Power Crisis Aftershock: The Potential Modification of Western Power Contracts* 9 (2007), http://www2.cera.com/westernpowercontracts (emphasizing need for predictable enforcement given that "investment decisions must be made years in advance of operation, and these decisions must recognize that under the long operating lives of these assets, capital cost recovery must span numerous market cycles").

[6] As Judge Posner explained, "a fixed-price contract is an explicit assignment of the risk of market price increases to the seller and the risk of market price decreases to the buyer * * * . [If] the buyer forecasts the market incorrectly and therefore finds himself locked into a disadvantageous contract, he has only himself to blame and so cannot shift the risk back to the seller * * *." *N. Ind. Pub. Serv. Co.* v. *Carbon County Coal Co.*, 799 F.2d 265, 278 (7th Cir. 1986).

Mobile decision recognized that preserving contract rates against after-the-fact challenge is critical to ensuring "the stability of supply arrangements which all agree is essential to the health of the * * * industry." 350 U.S. at 344. Just last Term, this Court rebuffed the Ninth Circuit's efforts to narrow the *Mobile-Sierra* doctrine, agreeing instead with FERC that "uncertainties regarding rate stability and contract sanctity can have a chilling effect on investments." *Morgan Stanley*, 128 S. Ct. at 2747 (quoting 72 Fed. Reg. 33,906-907). The *Mobile-Sierra* doctrine, the Court continued, is a "key source of stability" that reduces "volatility in the electricity markets" and thus "ultimately benefits consumers." 128 S. Ct. at 2749.

FERC too has repeatedly underscored *Mobile-Sierra*'s critical role. "Competitive power markets simply cannot attract the capital needed to build adequate generating infrastructure without regulatory certainty, including certainty that the Commission will not modify market-based contracts unless there are *extraordinary* circumstances." *Nev. Power Co.*, 99 FERC at 61,190. And *Mobile-Sierra* "has, if anything, become even more critical" in light of FERC's increasing reliance on markets and competition. *Ibid.* "The failure to protect parties' contractual expectations can harm customers by reducing the willingness of sellers and buyers to contract for rate certainty through fixed-rate contracts or by deterring sellers and buyers from making the investment needed to support the long-term contracts." *Californians for Renewable Energy, Inc.* v. *Cal. Pub. Utils. Comm'n*, 120 FERC ¶61,272 at 62,279 (2007).[7]

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[7] See also *Nev. Power Co.* v. *Enron Power Mktg., Inc.*, 103 FERC ¶61,353 at 62,393 (2003) (adopting ALJ's finding that "uncertainty [over] the enforceability of such contracts" would "erode investor confidence and willingness to invest in merchant energy projects, which, in turn, could have an adverse effect on infrastructure development").

B. The Court Of Appeals' Decision Upends *Mobile-Sierra* And Threatens Industry Stability

Notwithstanding the critical role that contract stability provides, the D.C. Circuit ruled that *Mobile-Sierra* provides protection only in a narrow category of cases—challenges brought by contractual counterparties—and provides no protection in challenges brought by non-parties. "[W]hen a rate challenge is brought by a non-contracting third party," that court held, "the *Mobile-Sierra* doctrine *simply does not apply*." Pet. App. 22a (emphasis added).

Left undisturbed, that "third-party exception" to *Mobile-Sierra*'s public-interest standard will engulf the rule and destroy the stability it is designed to provide. The decision would apply *Mobile-Sierra*'s presumption of reasonableness *only* to the two counterparties to the contract for the sale of power or natural gas. Literally *anyone else* that might be affected by a given contract would escape the presumption of reasonableness, including individual consumers, corporations, governmental entities, politicians, or state regulators. If any one of that boundless group of non-parties and potential surrogates asks FERC to abrogate a contract, they need not show, and FERC need not find, that the contract "seriously harm[s] the public interest." *Morgan Stanley*, 128 S. Ct. at 2743, 2746, 2748, 2750. It would be enough that the old rate looks "unjust" or "unreasonable" in light of new conditions—precisely the standard *Mobile-Sierra* and *Morgan Stanley* reject. Pet. App. 23a.

Subjecting fixed-price contracts to midstream abrogation if changing market conditions make one side of the contract (even temporarily) unattractive to any non-contracting entity destroys the purpose of those contracts. Such contracts could no longer serve as a "hedge" against spot-market volatility because, once that volatility arises, non-parties could challenge the contract rate as unreasonably low when compared to the then-

prevailing (much higher) market rates. Those expected to invest hundreds of millions of dollars developing new power plants will balk if the possibility of third-party challenges precludes them from relying on the promise to pay the contract price. Like the Ninth Circuit decision this Court reversed in *Morgan Stanley*, the decision below will "reduce the incentive" for both buyers and sellers to enter into long-term, fixed-price contracts. 128 S. Ct. at 2747. And as this Court observed in *Morgan Stanley*, consumers will suffer. "'[U]ncertainties regarding rate stability and contract sanctity can have a chilling effect on investments and a seller's willingness to enter into long-term contracts and this, in turn, can harm customers in the long run.'" *Id.* at 2749 (quoting 72 Fed. Reg. 39,906-907 (2007)).

This case illustrates precisely the dangers inherent in the court of appeals' new rule. FERC expressly approved the multiparty agreement here as just and reasonable, based on record evidence, after extensive litigation. Now, having litigated their objections to finality, non-parties will, if conditions change, get yet another chance to challenge the rates, exempt from the public-interest presumption. The resulting uncertainty is particularly problematic in connection with the auction pricing mechanism, which produces voluntary agreements to provide capacity three years in the future. See pp. 7-8, *supra*. That forward-capacity market is supposed to encourage new entrants to build additional generating capacity. To ensure that the promise to pay the amount set at auction provides an adequate incentive to invest the hundreds of millions necessary to build new capacity, the agreement provided *Mobile-Sierra* protection once the price is accepted by the buyer and seller through the auction process and is filed with FERC. But the promise to pay the auction amounts cannot provide the necessary incentive if the promise can be revisited continuously in light of changing circumstances. Only the

foolhardy (or those requiring enormous risk premiums) would invest millions to expand generation capacity with little certainty the contract price will be respected over the life of fixed-price agreement.

Nor will there be a shortage of non-contracting parties willing to challenge wholesale rate contracts. Because FERC regulates the middle of the distribution chain in both the electric and natural gas industries, there will always be interested non-parties as market conditions shift. If, in hindsight, the rate seems too high because the economy slips or demand declines, then retail customers, industrial buyers, state regulators and consumer advocates will step in to challenge the contract rate. If the rate seems too low because the economy heats up (or summer temperatures do), then an upstream supplier, lender, or any other entity interested in increasing contract prices—or avoiding what has become a money-losing contract—may likewise press for contract modification free from the dictates of the public interest presumption. The contract rate would be open to assault by interested parties on all sides.

One need look no further than the wake of this Court's decision in *Morgan Stanley* last Term to see the broad impact. One of the respondents in *Morgan Stanley* itself—the Office of the Nevada Attorney General, Bureau of Consumer Protection—was *not a party to the contract*. 128 S. Ct. at 2736. Following *Morgan Stanley*, moreover, this Court granted the petitions in companion cases, vacated the Ninth Circuit's judgment, and remanded for reconsideration in light of its decision. See 128 S. Ct. 2993 (mem.) (granting, vacating, and remanding *Pub. Utils. Comm'n of Cal.* v. *FERC*, 474 F.3d 587 (9th Cir. 2006), sub nom. *Sempra Generation* v. *Pub. Utils. Comm'n of Cal.* (No. 06-1454), and *Dynegy Power Mktg., Inc.* v. *Pub. Utils. Comm'n of Cal.* (No. 06-1468)). But the Ninth Circuit has now ordered briefing on

whether to apply the "third-party exception" to allow the complainants in those companion cases to avoid the public-interest presumption this Court articulated in *Morgan Stanley* instead of remanding the case to FERC. See *Pub. Utils. Comm'n of Cal.* v. *FERC*, No. 03-74207 (Oct. 20, 2008). It would be a rare case indeed where those seeking to evade *Mobile-Sierra* will be unable to find a non-party to join them in challenging the rates at issue.

The decision below has already created disarray in the industry and at FERC. Responding to that decision, FERC has adopted a new, nationwide policy that, if anyone files a contract that incorporates *Mobile-Sierra*'s public interest presumption, the contract must instead specify that it "imposes on non-contracting third parties the most stringent standard permissible under applicable law." *Duke Energy Carolinas, LLC*, 123 FERC ¶61,201 at 62,290 (2008).[8] No one knows exactly what that "most stringent standard" might be. But unless the decision below is reversed, it will *not* be the public-interest standard this Court reaffirmed in *Morgan Stanley*.[9]

The resulting "chilling effect on investments" could not come at a worse time. The electric and natural gas industries are highly capital intensive and fundamental to virtually all economic activity in this country. Over the next 15 years, the electric industry needs to invest an estimated $400 billion in new power plants and even more in additional infrastructure. See Makovich, *supra* note 5,

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[8] FERC has applied the new policy announced in *Duke Carolinas* in 38 orders or letter orders, 36 of which post-date this Court's decision in *Morgan Stanley*. See, *e.g.*, *S. Cal. Edison Co.*, 125 FERC ¶61,096 at 61,517 & n.3 (Oct. 27, 2008).

[9] The court of appeals' decision invites forum shopping as parties who want to preserve their *Mobile-Sierra* rights flee the decision below by seeking judicial review in other circuits. Energy companies and energy markets will thus confront profound uncertainty until this question is settled by this Court.

at 13-15. Contract certainty will be essential to support that massive new investment. By eviscerating the *Mobile-Sierra* doctrine, the decision below threatens that new investment precisely when it is needed most.

II. THE DECISION BELOW SQUARELY CONTRADICTS THIS COURT'S DECISION IN *MORGAN STANLEY* AND DECADES OF PRACTICE

The decision below did not merely eviscerate the *Mobile-Sierra* doctrine. It did so by invoking a legal theory that this Court rejected just last Term. It rejects FERC's position that *Mobile-Sierra* properly applies to non-party challenges. Pet. App. 200a & n.150 (listing cases); *id.* at 22a-23a. And it adopts a position that conflicts with decades of settled practice.

A. This Court Rejected The Rationale Of The Decision Below In *Morgan Stanley*

The court of appeals' holding that *Mobile-Sierra* does not apply to challenges by non-parties rests on the premise that the *Mobile-Sierra* doctrine is inconsistent with the "just and reasonable" standard found in FPA §206. The court of appeals rejected application of *Mobile-Sierra* to non-party challenges because it would "deprive them of their statutory right to challenge rates under the 'just and reasonable' standard." Pet. App. 19a. "[T]he relevant statutory language," the court held, "is quite clear" in that it requires "just and reasonable" review. *Id.* at 23a-24a. The court of appeals found that *Mobile-Sierra* "carve[d] out an exception" to the statutory "just and reasonable" standard based on contract principles. *Id.* at 20a. The court of appeals therefore ruled that *Mobile-Sierra*'s public-interest test is an "illegal standard" that "deprives non-settling parties of their statutory right" to have future "rate challenges adjudicated under the" statutory "'just and reasonable standard' * * * in cases of changed circumstances." *Id.* at 22a-23a.

That holding cannot be reconciled with this Court's subsequent decision in *Morgan Stanley*. That decision flatly rejected the view that *Mobile-Sierra* departs from the statutory "just and reasonable" standard. Rather, this Court held that there "is only one statutory standard for assessing wholesale electricity rates, whether set by contract or tariff—the just-and-reasonable standard." 128 S. Ct. at 2745. The *Mobile-Sierra* test, this Court held, merely represents the "mode of review" employed in the context of negotiated contract rates:

> Over the years, the Commission began to refer to the two modes of review—one with the *Mobile-Sierra* presumption and the other without—as the "public interest standard" and the "just and reasonable standard." Decisions from the Courts of Appeals did likewise. We do not take this nomenclature to stand for the obviously indefensible proposition that a standard different from the statutory just-and-reasonable standard applies to contract rates. Rather, the term "public interest standard" refers to the differing *application* of that just-and-reasonable standard to contract rates.

128 S. Ct. at 2740 (citations omitted). "*Sierra* thus provided a definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context * * * ." *Id.* at 2746.

The decision below thus adopted the very position this Court rejected in *Morgan Stanley*. Indeed, it adopted the position of the *Morgan Stanley* dissent, which characterized *Mobile-Sierra*'s presumption of reasonableness as a judicial invention based on an "atextual reading of [FPA] §§ 205 and 206." 128 S. Ct. at 2754 (Stevens, J., dissenting). But the majority rejected that view, finding that "the dissent's interpretation, whatever plausibility it has as an original matter, cannot be squared with *Sierra*, which plainly distinguished between unilaterally and bi-

laterally set rates, and said that the only relevant consideration for the Commission in the latter case is whether the public interest is harmed." *Id.* at 2749 n.6.

The decision below also commits precisely the same error the Ninth Circuit committed in *Morgan Stanley*: treating *Mobile-Sierra* as "the equivalent of an estoppel doctrine" that applies to contract counterparties (who voluntarily assume an obligation) but to no one else. See *Morgan Stanley*, 128 S. Ct. at 2746. As *Morgan Stanley* makes clear, *Mobile-Sierra* is not an estoppel doctrine. Instead, it is a construction of the FPA that rests on two insights. First, "[i]n wholesale markets, the party charging the rate and the party charged [are] often sophisticated businesses enjoying presumptively equal bargaining power, who could be expected to negotiate a 'just and reasonable' rate as between the two of them." 128 S. Ct. at 2746 (quotation marks omitted). As a result, FERC must "presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law." *Id.* at 2737. There is no reason that presumption would disappear based on the identity of the challenging party. Second, contract stability and predictability are critical to the health of the market. *Id.* at 2749. There is no reason why instability caused by non-party challenges should be more acceptable than instability caused by party challenges. The square conflict between this case and *Morgan Stanley* is itself grounds for further review. At the very least, the Court should grant the petition, vacate the decision below, and remand the case to give the court of appeals an opportunity to reconsider the matter on a fresh slate in light of this Court's intervening decision in *Morgan Stanley*.

B. The Decision Below Conflicts With Decades Of Settled Practice On An Important Issue

For generations, interpretation of the *Mobile-Sierra* doctrine was "so uniform" and "settled" that this Court

had no reason to intervene until it became necessary to overturn the Ninth Circuit's "erroneous decision" in *Morgan Stanley* last Term. 128 S. Ct. at 2749 n.6. Over the past 8 years, FERC has relied on *Mobile-Sierra* more than 600 times; and the federal courts have invoked it in scores of decisions. *Morgan Stanley*, 128 S. Ct. at 2749 n.6. Yet we know of no court that has ever before held that the doctrine was inapplicable to third-party challenges. To the contrary, it has long been understood that *Mobile-Sierra* protects contract rates from all challenges—whether by parties or non-parties, including FERC acting *sua sponte*.

Thus, in *Northeastern Utilities Service Co.* v. *FERC*, 993 F.2d 937, 961-962 (1st Cir. 1993), and *Boston Edison Co.* v. *FERC*, 233 F.3d 60, 68 (1st Cir. 2000), the First Circuit held that when FERC—which is not a contracting party—seeks to challenge a contract rate as unjust or unreasonable, FERC too must overcome the *Mobile-Sierra* presumption. It is simply impossible to reconcile the requirement that FERC overcome the *Mobile-Sierra* presumption with the putative rule that *Mobile-Sierra* applies only to party challenges. Nor does it make any sense that FERC, the federal regulator charged with protecting the public interest in this area, would have to show serious harm to the public interest under *Mobile-Sierra* to overturn a contract rate, but a State Attorney General or a ratepayer, with no expertise or congressional mandate, would not. The fact is that the *Mobile-Sierra* standard has, until now, applied to all challenges to contract rates, regardless of who brings them.

Courts have routinely applied *Mobile-Sierra* to non-party challenges in the context of "undue discrimination" claims as well. For example, in *Boroughs of Chambersburg* v. *FERC*, 580 F.2d 573, 577-78 (D.C. Cir. 1978), a wholesale supplier filed rate increases that had different

impacts on customers depending on whether their contracts were subject to *Mobile-Sierra* protection. The disadvantaged customer (who lacked *Mobile-Sierra* protection) sought to invalidate the favored customer's contract, urging that the differential treatment was unduly discriminatory. The court of appeals rejected that claim, finding no undue discrimination because the utility was free to raise the non-settling parties' rates, but the settling parties' rate contracts were protected under *Mobile-Sierra*. *Chambersburg*, 580 F.2d at 577-78. In *Public Service Co. of Indiana, Inc.* v. *FERC*, 575 F.2d 1204, 1211-13 & n.12 (7th Cir. 1978), the Seventh Circuit similarly rejected a non-party's effort to challenge another customer's contract as discriminatory in light of *Mobile-Sierra*. Later that year, the D.C. Circuit in turn relied on *Chambersburg* and the Seventh Circuit's decision in *PSCI* to reach the same conclusion in *Town of Norwood* v. *FERC*, 587 F.2d 1306, 1310-14 (D.C. Cir. 1978). "[I]t is possible to have discrimination that violates §205(b)," the court ruled, "but does not dismantle the protection generally afforded to fixed-rate contracts under *Mobile-Sierra*" in challenges brought by third parties under FPA §206(a). 587 F.2d at 1314 n.21.

Just last year, the D.C. Circuit rejected an effort by non-contracting third parties to challenge FERC's more favorable treatment of certain grandfathered agreements under a new tariff regime, and rebuffed their claim that such agreements discriminated against them and shifted costs to non-contracting parties in violation of FPA §205. *Wis. Pub. Power Inc.* v. *FERC*, 493 F.3d 239, 270, 274 (D.C. Cir. 2007). The court held that the challengers had failed to show that modification of the grandfathered agreements was required by the "public interest" or that the alleged cost shifts imposed an "excessive burden" under the *Mobile-Sierra* doctrine. See *id.* at 273-75 (relying on *Norwood*, 587 F.2d at 1314 n.21). The federal courts thus have repeatedly invoked *Mobile-Sierra* to

reject the efforts of non-parties to invalidate (as discriminatory or unjust) the contracts of others. Those cases would make no sense if "the *Mobile-Sierra* doctrine simply does not apply" to challenges "brought by a non-contracting third party." Pet. App. 22a.

C. The Court Of Appeals' Decision Conflicts With Other Applicable Decisions And Principles

For the reasons given above, the court of appeals' reasoning cannot be reconciled with this Court's decision in *Morgan Stanley* or with *Mobile-Sierra*'s origins or purposes. See pp. 16-20, *supra*. Nowhere did the court of appeals explain why the presumption of reasonableness that arises from a negotiated contract, or the need for contract stability to encourage investment, would evaporate based on the identity of the challenging party. *Ibid.* But the court of appeals' decision is difficult to reconcile with this Court's precedents and general legal principles in other respects as well.

1. As an initial matter, the court of appeals' conclusion that *Mobile-Sierra* does not apply to non-contracting parties is difficult to reconcile with the test that *Mobile* and *Sierra* establish. The public-interest test under *Mobile-Sierra* is by its terms targeted to protecting non-contracting parties. *Sierra* listed three examples of where a contract might be contrary to the public interest: "where [the contract] might impair the financial ability of the public utility to continue its service, *cast upon other consumers an excessive burden, or be unduly discriminatory*." 350 U.S. at 354-55 (emphasis added). The last two factors expressly consider the impact on non-contracting third parties. *Morgan Stanley* similarly focuses the public interest presumption on preventing "serious[] harm[]" to "the public," 128 S. Ct. at 2737—by definition an aggregate group of non-contracting third parties. It thus cannot be correct that "the *Mobile-Sierra* doctrine simply does not apply" to non-contracting third parties. Pet. App. 22a. It always has. Indeed, the

Mobile-Sierra standard is predicated on the protection of non-parties' interests.

2. Second, in *Morgan Stanley*, this Court made clear that *Mobile-Sierra*, far from being a limit on contracting parties' efforts to escape their obligations, is a limit on *FERC's authority* to abrogate or modify contract rates. Every mention of the *Mobile-Sierra* presumption in *Morgan Stanley* is formulated as a limit on *FERC's* authority. See, *e.g.*, 128 S. Ct. at 2737 ("Under the *Mobile-Sierra* doctrine, [FERC] must presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law."); *id.* at 2745 ("[W]e conclude that the *Commission* was required, under our decision in *Sierra*, to apply the *Mobile-Sierra* presumption in its evaluation of the contracts here.").

Mobile-Sierra thus does nothing to prevent interested persons from filing a complaint at FERC contending that a rate is unjust and unreasonable. But where a rate is set by contract, FERC must presume the contract rate is reasonable, absent "extraordinary circumstances" or "unequivocal public necessity," because "the FPA intended to reserve the Commission's contract-abrogation power for those extraordinary circumstances where the public will be severely harmed." 128 S. Ct. at 2749. Likewise, the *Mobile-Sierra* clause in the agreement at issue here does not interfere with any statutory rights. No one is prevented from urging that a rate is unjust and unreasonable within the meaning of FPA § 206 if at some future date the transition rates or the auction results seem unreasonable. The agreement simply makes clear that, in deciding whether the rate is just and reasonable, FERC must apply the *Mobile-Sierra* presumption that the rate is reasonable unless that presumption is overcome by compelling proof of severe harm to the public

interest. FERC has approved contracts with such clauses for years.[10]

3. Without addressing any of the foregoing, the court of appeals held that "the *Mobile-Sierra* doctrine simply does not apply" to non-party challenges based on its assertion that "a contract cannot bind a nonparty." Pet. App. 22a (quoting *Waffle House*, 534 U.S. at 294). But the premise that *Mobile-Sierra* derives from, and is bounded in scope by, contract law is incorrect. *Mobile-Sierra* comes from the FPA, and its application to FERC-jurisdictional agreements must be determined by that statute. See pp. 23-26, *supra*. To the extent contract principles are relevant, however, they undercut the D.C. Circuit's view.

As an initial matter, *Waffle House* held that an arbitration agreement between an employer and an employee could not prevent the EEOC from *bringing a complaint* against the employer in its own name. 534 U.S. at 295-96 (finding the agreement did not effect "a waiver of a nonparty's statutory remedies"). But *Waffle House* left "open" whether "a settlement or arbitration judgment would affect the validity of the EEOC's claim or the character of relief the EEOC may seek." *Id.* at 297. That distinction is key. This Court has long held that an agreement will not be read to "bind" third parties merely because it will affect them negatively (even profoundly so). *See Local No. 93, Int'l Ass'n of Firefighters* v. *City of Cleveland*, 478 U.S. 501, 529-30 (1986). Thus, while the application of the public-interest presumption necessarily *affects* any attempt by a non-contracting third party to

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[10] FERC and FPC cases reviewing *Mobile-Sierra* provisions in contracts and settlement agreements are too numerous to list. See, *e.g.*, Pet. App. 200a & n.150 (listing recent examples). This year alone, FERC has already issued more than 50 decisions accepting, rejecting, or modifying such provisions in contracts and settlement agreements. This process has, of course, become more difficult since the decision below issued. See note 8, *supra*.

modify or abrogate a contract, the contract itself does not bind them. Instead, under *Mobile-Sierra* and *Morgan Stanley*, the contract produces a presumption that binds *FERC* in its analysis of whether the rate is just and reasonable.

In any event, the court of appeals' analysis is upside-down even as a matter of contract law. While non-parties are not bound by a contract, they also ordinarily lack standing to challenge contract terms—even if those terms somehow affect them. *In re Vic Supply Co.*, 227 F.3d 928, 931 (7th Cir. 2000) ("Obviously the fact that a third party would be better off if a contract were unenforceable does not give him standing to sue to void the contract."). Here, the contract provision establishing the standard of review may *affect* later challenges by the non-settling parties, but it "does not bind [them] to do or not to do anything," "imposes no legal duties or obligations on [them] at all," and "does not purport to resolve any claims the[y] might have." *Firefighters*, 478 U.S. at 529-30. Yet the court of appeals afforded non-parties to the contract at issue a right to challenge contract terms in light of changed circumstances that is more expansive than the right enjoyed by the contracting parties themselves. That result is at odds with common law and common sense.

CONCLUSION

The petition for a writ of certiorari should be granted. At the very least, the Court should grant the petition, vacate the decision below in relevant part (Part IV), and remand for reconsideration in light of this Court's intervening decision in *Morgan Stanley*.

Respectfully submitted.

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November 21, 2008

APPENDIX

APPENDIX A

IN THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

NOS. 06-1403, 06-1427, 07-1193

MAINE PUBLIC UTILITIES COMMISSION,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent.

CONNECTICUT DEPARTMENT OF PUBLIC UTILITY CONTROL, *et al.*,
Intervenors.

On Petitions for Review of Orders of the Federal Energy Regulatory Commission

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ARGUED FEB. 14, 2008.
DECIDED MARCH 28, 2008.

Before: ROGERS and GARLAND, Circuit Judges, and SILBERMAN, Senior Circuit Judge.

PER CURIAM:

The consolidated petitions for review challenge FERC's approval of a comprehensive settlement that redesigned New England's capacity market. The Maine Public Utilities Commission and the Attorneys General of Connecticut and Massachusetts assert that FERC's

approval of the settlement was arbitrary and capricious, contrary to law, and beyond the Commission's jurisdiction. We reject most of these arguments, but we agree with the petitioners that the Commission has unlawfully deprived non-settling parties of their rights under the Federal Power Act.

I.

In a "capacity" market—as opposed to a wholesale electricity market—"the [transmission provider] compensates the generator for the *option* of buying a specified quantity of power irrespective of whether it ultimately buys the electricity."[1] *Keyspan-Ravenswood, LLC v. FERC*, 474 F.3d 804, 806 (D.C. Cir. 2007). In order to maintain the reliability of the grid, transmission providers generally purchase more capacity than is necessary to meet their customers' demand for electricity. This ensures that the transmission providers are able to respond adequately to unexpected fluctuations in demand.

For many years, New England's capacity market has been rife with problems. As the Commission explained in 2003, "existing generators needed for reliability are not earning sufficient revenues (and are in fact losing money), and [ ] additional infrastructure is needed soon to avoid violations of reliability criteria." *Devon Power LLC*, 115 FERC ¶ 61,340 at 62,315 (2006). In other words, the supply of capacity was barely sufficient to meet the region's demand.

FERC, the generators, the transmission providers, and the power customers have made several attempts to address these issues. In 2003, a group of generators sought to enter into "Reliability Must-Run" agreements

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[1] It would have been helpful if the parties had actually defined "capacity" before delving into the intricacies of New England's capacity market. Also, the briefs would have been much easier to read if the parties had used fewer acronyms.

with the New England Independent System Operator ("ISO"), which operates the transmission system in New England.[2] Under a Must-Run agreement, a financially-troubled generator in an area with supply shortages may recover up to its full cost-of-service in order to remain in operation. Those agreements have several important drawbacks. As FERC explained:

> [Must-Run] contracts suppress market-clearing prices, increase uplift payments, and make it difficult for new generators to profitably enter the market. . . . [E]xpensive generators under [Must-Run] contracts receive greater revenues than new entrants, who would receive lower revenues from the suppressed spot market price. In short, extensive use of [those] contracts undermines efficient market performance.

Devon Power LLC, 103 FERC ¶ 61,082 at 61,270 (2003). For these reasons, FERC accepted the Must-Run agreements filed by the New England generators, but only allowed these generators to recover certain maintenance costs, not their full cost-of-service. *Id.* at 61,270-71.

In its orders addressing the Must-Run agreements, the Commission simultaneously directed the ISO to develop a new market mechanism that would include a

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[2] An ISO is an independent company that has operational control, but not ownership, of the transmission facilities owned by member utilities. ISOs "provide open access to the regional transmission system to all electricity generators at rates established in a single, unbundled, grid-wide tariff . . . ." *Midwest ISO Transmission Owners v. FERC*, 373 F.3d 1361, 1364 (D.C. Cir. 2004) (citation omitted). In 2004, the New England ISO was organized as a Regional Transmission Organization ("RTO"). RTOs are given greater regulatory flexibility by FERC, provided that they (*inter alia*): are regional in scope, have exclusive operational control over all transmission facilities within their control, and have sole authority to approve or deny requests for transmission service. *Id.* at 1365.

location requirement. *Id.* at 61,271. In a locational market, prices are set separately for various geographical sub-regions. Thus, prices would be highest in the regions with the most severe capacity shortages, which would encourage new entry.

In response to FERC's directive, the ISO proposed a locational capacity market structure in March 2004. This proposed market mechanism included four sub-regions, each of which would have a monthly auction for capacity. The auctions would be based on an "administratively-determined demand curve" that would establish the price and quantity of capacity that must be procured within each sub-region.[3] *Devon Power LLC*, 107 FERC ¶ 61,240 at 62,022 (2004). FERC commended the ISO for adopting a locational pricing mechanism that took account of transmission constraints between different subregions within New England. *Id.* at 62,028. However, the demand curve proposed by the ISO was extremely controversial—numerous parties submitted comments and testimony regarding the proper height and slope of the curve. *Id.* at 62,031. FERC set the matter for hearing before an Administrative Law Judge ("ALJ").

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[3] Although the parties refer to this as a "demand curve," that term is misleading. Normally, a "demand curve" is a model of the relationship between prices and consumer preferences in a free market. In contrast, the "demand curve" proposed by the ISO is an entirely artificial construct that specifies the prices that must be paid for various quantities of capacity. 107 FERC at 62,022; *see also Elec. Consumers Res. Council v. FERC*, 407 F.3d 1232, 1234-35 (D.C. Cir. 2005) (explaining the construction of a similar "demand curve" by the New York ISO). This proposal was intended to make revenues and price movements more stable and predictable. 107 FERC at 62,022. That may or may not have been sound policy, but it more accurately should be termed a "non-demand demand curve" reminiscent of the once regulatory invention, a "non-bank bank."

In June 2005, the ALJ issued a 177-page order that largely accepted the ISO's proposed demand curve. *Devon Power LLC*, 111 FERC ¶ 63,063 (2005). Several parties filed exceptions to this decision, arguing that the ALJ wrongfully excluded evidence and failed to respond to comments about flaws in the ISO's demand curve. On September 20, 2005, the full Commission held an all-day oral argument on the locational market structure and the proposed demand curve. FERC subsequently established settlement procedures to allow the parties to develop a new market mechanism.

After four months of negotiations involving 115 parties, a settlement was reached. As FERC has repeatedly reminded us, only eight of these parties opposed the final settlement. 115 FERC at 62,306. The key feature of the settlement agreement is the Forward Capacity Market, which would replace the ISO's earlier proposal and eliminate the need for the controversial demand curve. Under the Forward Market, there will be annual auctions for capacity, which will be held three years in advance of when the capacity is needed. *Id.* The settling parties determined that a three-year lead time will "provide for a planning period for new entry and allow potential new capacity to compete in the auctions." *Id.* Each transmission provider will be required to purchase enough capacity to satisfy its "installed capacity requirement," which is the minimum level of capacity that is necessary to maintain reliability on the grid. *Id.* at 62,307. As FERC requested, the Forward Market also includes a locational component—the annual auctions will be held in different "capacity zones" based on transmission constraints between the various sub-regions within New England. *Id.*

The most contentious issue regarding the Forward Market is the set of "transition payments" that will be required from December 1, 2006 until June 1, 2010. As

explained above, the Forward Market provides for a three-year lead time in the capacity auctions, in order to allow new entrants to bid in the auctions. However, this leaves a three-year gap between the first auction and the time when the capacity procured in this auction will be provided. The parties addressed this issue by negotiating a series of fixed payments that will be paid to generators during the transition period. 115 FERC at 62,308. The agreement also provides that challenges to the transition payments and the final Forward Market auction clearing prices—regardless of whether the challenge is brought by a settling party, a non-settling party, or the Commission—will be adjudicated under the highly-deferential "public interest" standard rather than the usual "just and reasonable" standard. *Id.* at 62,332-33.

On June 16, 2006, FERC approved the settlement agreement, finding that "as a package, it presents a just and reasonable outcome for this proceeding consistent with the public interest." *Id.* at 62,304. Most importantly, the Commission determined that the settlement would address the problems that had plagued New England's capacity market:

> The settlement package, including both the [Forward Market] and the interim transition mechanism, resolves the issues raised in this proceeding concerning the under-compensation of capacity resources in New England, and provides the appropriate market structure to ensure that generating resources are appropriately compensated based on their location and contribution to system reliability and provides incentives to attract new infrastructure where needed.

Id. at 62,316. FERC conceded that the transition payments were not ideal "as a single market design element," but concluded that they were a "reasonable transitory mechanism that enables the New England

region to shift to the [Forward Market]." *Id.* at 62,319. In particular, the Commission determined that the transition payments "fall at the very low end" of the range of demand curves (prices) submitted by Maine and the ISO during the litigation over the ISO's previous market structure proposal. *Id.* at 62,321. FERC also approved the agreement's incorporation of the "public interest" standard of review because use of the more deferential standard in a limited number of circumstances would promote "rate stability." *Id.* at 62,335.

After FERC denied rehearing, the Maine Public Utilities Commission and the Attorneys General of Connecticut and Massachusetts petitioned for review, arguing that the Commission's approval of the settlement was arbitrary and capricious, contrary to law, and beyond the scope of FERC's jurisdiction.[4] Specifically, petitioners assert that: (1) FERC's acceptance of the transition payments was arbitrary and capricious because the record did not contain sufficient data about generators' costs; (2) FERC unreasonably accepted the transition payments even though the payments did not include a locational pricing mechanism; (3) FERC unlawfully accepted a "*Mobile-Sierra*" provision that imposed the deferential "public interest" standard of review on rate challenges brought by non-settling parties; and (4) FERC lacks jurisdiction to approve the settlement agreement because the Forward Market will effectively force states to acquire a specific level of capacity. For the reasons set forth below, we grant the petition for review with respect to the *Mobile-Sierra* issue, but we deny the petition with respect to the other three issues.

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[4] The orders under review are *Devon Power LLC*, 115 FERC ¶ 61,340 (2006); *Devon Power LLC*, 117 FERC ¶ 61,133 (2006); *ISO New England, Inc.*, 117 FERC ¶ 61,132 (2006); and *ISO New England, Inc.*, 119 FERC ¶ 61,044 (2007).

II.

The petitioners argue that FERC's approval of the settlement's transition payments was arbitrary and capricious, in violation of the Administrative Procedure Act, 5 U.S.C. § 706(2)(A). To withstand review under that standard, FERC must have "examine[d] the relevant data and articulate[d] a satisfactory explanation for its action including a 'rational connection between the facts found and the choice made.'" *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43, 103 S. Ct. 2856, 77 L. Ed. 2d 443 (1983) (quoting *Burlington Truck Lines, Inc. v. United States*, 371 U.S. 156, 168, 83 S. Ct. 239, 9 L. Ed. 2d 207 (1962)). The Commission's findings of fact, "if supported by substantial evidence," are conclusive. 16 U.S.C. § 825*l*(b). When the record would support more than one outcome, we must uphold FERC's order because "[t]he question we must answer . . . is not whether record evidence supports [the petitioner's desired outcome], but whether it supports FERC's." *Fla. Mun. Power Agency v. FERC*, 315 F.3d 362, 368 (D.C. Cir. 2003). *See generally NorAm Gas Transmission Co. v. FERC*, 148 F.3d 1158, 1162 (D.C. Cir. 1998) ("[I]n reviewing the Commission's approval of a contested settlement, we must determine whether the Commission has supplied a 'reasoned decision' that is supported by 'substantial evidence.'" (quoting 18 C.F.R. § 385.602(h)(1)(i))).

In this case, after considering the merits of the settlement as a whole, FERC examined the record evidence and concluded that the transition payments fell within a "reasonable range of capacity prices." 115 FERC at 62,319. The Commission correctly noted that there is not a single "just and reasonable rate" but rather a zone of rates that are just and reasonable; a just and reasonable rate is one that falls within that zone. *Id.*; *see Montana-Dakota Utils. Co. v. N.W. Pub. Serv. Co.*, 341 U.S. 246,

251, 71 S. Ct. 692, 95 L. Ed. 912 (1951) ("Statutory reasonableness is an abstract quality represented by an area rather than a pinpoint. It allows a substantial spread between what is unreasonable because too low and what is unreasonable because too high."); *Pac. Gas & Elec. Co. v. FERC*, 306 F.3d 1112, 1116 (D.C. Cir. 2002) ("[T]he court may only set aside a rate that is outside a zone of reasonableness, bounded on one end by investor interest and the other by the public interest against excessive rates."); *cf. In re Permian Basin Area Rate Cases*, 390 U.S. 747, 767, 88 S. Ct. 1344, 20 L. Ed. 2d 312 (1968) ("[T]his Court has often acknowledged that the Commission is not required by the Constitution or the Natural Gas Act to adopt as just and reasonable any particular rate level; rather, courts are without authority to set aside any rate selected by the Commission which is within a 'zone of reasonableness.'"); *ExxonMobil Gas Mktg. Co. v. FERC*, 297 F.3d 1071, 1084 (D.C. Cir. 2002) ("The burden is on the petitioners to show that the Commission's choices are unreasonable and its chosen line of demarcation is not within a zone of reasonableness as distinct from the question of whether the line drawn by the Commission is precisely right." (internal quotation marks omitted)).

In challenging FERC's decision to approve the transition payments, the petitioners argue that there was no record evidence of existing generators' costs and that without such evidence FERC could not find that the payments fell within a reasonable range of capacity prices. In its early orders in *Devon Power*, however, FERC determined that reliance on individualized cost recovery proceedings was not a policy in the public interest and that, instead, capacity payments should be made to all suppliers with a single market-clearing price. *See, e.g., Devon Power LLC*, 110 FERC ¶ 61,315 at 62,227 (2005). FERC is correct that it need not rely on generators'

costs to determine rates. The Supreme Court has disavowed the notion that rates must depend on historical costs and has held that rates may be determined by a variety of formulae. *See, e.g., FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 602, 64 S. Ct. 281, 88 L. Ed. 333 (1944) ("[T]he Commission [i]s not bound to the use of any single formula or combination of formulae in determining rates."); *see also Mobil Oil Corp. v. FPC*, 417 U.S. 283, 316, 94 S. Ct. 2328, 41 L. Ed. 2d 72 (1974) ("Mobil's argument assumes that there is only one just and reasonable rate possible for each vintage of gas, and that this rate must be based entirely on some concept of cost plus a reasonable rate of return. We rejected this argument in *Permian Basin* and we reject it again here."); *Am. Pub. Power Ass'n v. FPC*, 522 F.2d 142, 146 (D.C. Cir. 1975) ("Congress carefully eschewed tying 'just and reasonable' rates to any particular method of deriving the rates. Certainly there is nothing in the Federal Power Act specifically endorsing historic test year ratemaking or any other technique of ratemaking. Congress clearly intended to allow the Commission broad discretion in regard to the methodology of testing the reasonableness of rates.").[5]

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[5] The petitioners cite *NSTAR Electric & Gas Corp. v. FERC*, 481 F.3d 794 (D.C. Cir. 2007), for the proposition that FERC cannot approve a rate without reviewing cost data, but this mischaracterizes the holding of that case. In *NSTAR*, FERC approved contracts between ISO-New England and certain generators because those contracts provided compensation to generators at a percentage of fixed or variable costs. We remanded the case because, although FERC's rationale relied on costs, there was no substantial evidence of those costs in the record. The *NSTAR* court specifically recognized, however, that FERC need not always rely on historic cost data. *See id.* at 804 ("Nor, of course, do we mean to suggest that only prices in line with historic accounting costs would qualify as just and reasonable.").

Of course, FERC cannot pluck rates out of thin air; it must rely on record evidence to establish a reasonable range of rates. But contrary to the petitioners' suggestion, FERC's statement that "the transition payments are reasonable rates for existing generators until the [Forward Market] begins," 115 FERC at 62,321, was not simply an assertion but rather a conclusion based on the Commission's analysis of two pieces of record evidence: (1) projected prices under demand curves introduced by Maine and Vermont load representatives and by ISO—New England at the hearing on the locational installed capacity mechanism, and (2) the estimated cost of entry for a new peaker unit. Only after reviewing this evidence to establish a "zone of reasonableness" did FERC conclude that the transition payments fell within the zone. *Id.*; *see also* 117 FERC at 61,718 (discussing FERC's reliance on demand curve and cost of new entry evidence in evaluating the transition payments).

In establishing the reasonable range of capacity prices, FERC first reviewed evidence introduced at the hearing on the locational installed capacity mechanism (which was later replaced by the Forward Market). FERC decided to look at projected prices for Maine and Northeastern Massachusetts under both the demand curve proposed by Maine and Vermont load representatives and the demand curve proposed by the ISO. The Commission acknowledged that these were not the only two demand curves proposed at the hearing, but, as it explained more fully in the order on rehearing, it chose to rely on these two curves because they came from two different sectors. Load representatives offered demand curves that projected low prices, while supplier representatives offered demand curves that projected high prices; thus, FERC noted that "[i]f the Commission relied only upon demand curves proposed by parties representing load, the transition payments may have appeared

excessive; relying only on demand curves proposed by suppliers would imply that the transition payments were inadequate." 117 FERC at 61,719. FERC accordingly "conclude[d] that relying on proposed demand curves from a single sector would have been unreasonable" and focused on two curves—from two different sectors—that provided a narrow range of price projections. *Id.*; *see also* 115 FERC at 62,319-20. Comparing the transition payments to these demand curve projections, FERC found that the transition payments fell within the range of capacity prices projected by both demand curves. 115 FERC at 62,321.

The petitioners object that FERC improperly relied on the demand curves as a basis of comparison because FERC did not expressly find them to be just and reasonable. Since it never made that finding, the petitioners insist, FERC could not rely on the demand curves to find that the transition payments were reasonable. It is true that FERC may not use unexamined rates as a basis of comparison. *Cf. Laclede Gas Co. v. FERC*, 997 F.2d 936, 946-47 (D.C. Cir. 1993). But here, FERC examined the record evidence and concluded that these two curves "establishe[d] a reasonable range of capacity prices for comparison." 117 FERC at 61,719; *see also* 115 FERC at 62,319-21. FERC's determination that these curves offered a reasonable range of prices for comparison was further supported both by the fact that FERC had explicitly endorsed the demand curve approach in earlier orders, *see* 110 FERC at 62,221 ("[W]e preliminarily find the use of ICAP regions and an ICAP demand curve as proposed by ISO-NE to be just and reasonable . . . ."); *Devon Power LLC*, 107 FERC ¶ 61,240 at 62,031 (2004) ("We agree with ISO-NE's overarching proposal to use a demand curve, and in particular a downward sloping demand curve, as part of the eventual LICAP mechanism in New England."), and by the fact that the administra-

tive law judge had adopted the ISO's demand curve—which contained higher price projections than the Maine-Vermont curve—after a lengthy proceeding, *Devon Power LLC*, 111 FERC ¶ 63,063 at 65,217 (2005) ("[T]he undersigned finds the ISO's demand curve proposal to be just and reasonable . . . ."); *see* 115 FERC at 62,319 ("[T]he Initial Decision did adopt ISO-NE's proposal . . . ."); *see also id.* at 62,320-21. In light of this evidence, FERC's determination was sufficient. A binding merits decision was not required; indeed, such a requirement would largely vitiate the purpose of a settlement.

The petitioners also object to FERC's reliance on evidence of the estimated cost of new entry to determine a reasonable range of rates. The petitioners raise two concerns. First, they argue that cost of new entry represents the estimated costs of a new peaker, not those of an existing generator, and that the two may have different capital costs. The Commission determined, however, that new peakers have "capital costs [that] are lower than most, if not all, other plants." 115 FERC at 62,321. Hence, if cost of new entry is used as a reference point, the transition payments "are likely to be significantly lower than a cost-of-service payment for most, if not all, new generators." *Id.*; *see id.* at 62,319 (concluding that "in the first years," the transition "payments are less than the cost of new entry, accurately reflecting market conditions").

Second, the petitioners argue that cost of new entry is an arbitrary reference point for the transition period because, although cost of new entry provides a starting point for the Forward Market auction, the Forward Market does not exist during the transition period. But the fact that cost of new entry is used to kick off the auction does not mean that it is relevant only for that purpose. If anything, the reliance on cost of new entry as a starting point of the Forward Market auction underscores its rel-

evance to appropriate rates: it is used to commence the auction because it approximates reasonable compensation for existing as well as new generators. *See id.* at 62,326. FERC sets rates to ensure both that existing generators are adequately compensated and that prices support new entry when additional capacity is needed. *See, e.g.*, Recording of Oral Arg. at 1:02:34-1:03:01, 1:09:30-1:10:35. As FERC therefore noted, cost of new entry is "a key factor in determining appropriate rates for capacity" and was central to the demand curves under the locational installed capacity market as well as the Forward Market design. 117 FERC at 61,718; *cf. Elec. Consumers Res. Council v. FERC*, 407 F.3d 1232, 1235, 1237-38 (D.C. Cir. 2005) (upholding FERC's approval of a demand curve that sets prices based on the annualized cost of a new peaker plant); *New York Indep. Sys. Operator, Inc.*, 117 FERC ¶ 61,086 at 61,443 n.7 (2006) ("In a competitive market, prices should reach equilibrium at or near to the levelized net cost of new entry."). We conclude that it was reasonable for the Commission to look to cost of new entry as a basis of comparison in its review of the transition payments.

Finally, the petitioners claim that FERC did not respond meaningfully to their objections to the transition payments. *See PPL Wallingford Energy LLC v. FERC*, 419 F.3d 1194, 1198 (D.C. Cir. 2005) ("An agency's 'failure to respond meaningfully' to objections raised by a party renders its decision arbitrary and capricious." (quoting *Canadian Ass'n of Petroleum Producers v. FERC*, 254 F.3d 289, 299 (D.C. Cir. 2001))). Specifically, the petitioners argue that FERC did not address the argument of the Attorneys General that the transition payments do not reflect market conditions, reliability contributions, or cost-of-service; and they cite witness that the transition payments are significantly in excess of what is needed to retain existing resources because many

generators rely in part on sources of energy other than oil and gas (e.g., nuclear and hydro power). The Commission did, however, respond to these objections, discussing the long-term commitment and enhanced reliability contributions of generators that the transition payment mechanism requires. *See* 115 FERC at 62,322; 117 FERC at 61,720, 61,724. FERC also rejected the petitioners' premise that their expert's testimony was the only relevant evidence about whether the transition payments were reasonable and explained that cost of new entry and the demand curves were relevant evidence. *E.g.*, 117 FERC at 61,718-20. In short, FERC's conclusion that the transition payments fell within a reasonable range of capacity prices was a reasoned decision supported by substantial evidence.[6]

III.

Petitioner Maine Public Utilities Commission (Maine PUC) argues that FERC's acceptance of non-locational pricing during the transition period was arbitrary and capricious, attacking FERC's decision on both general and specific grounds.

At a general level, Maine PUC contends that FERC acted arbitrarily in approving non-locational transition payments when FERC had previously insisted that a locational structure was necessary for New England.

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[6] The petitioners also argue that FERC acted arbitrarily and capriciously in ordering an overbroad remedy to the market problem it had identified. According to the petitioners, the ongoing use of Reliability Must-Run contracts during the transition period contravenes FERC's initial desire to implement a market structure to replace Must-Run contracts. This objection was not raised before the agency and is therefore waived. *See* 16 U.S.C. § 825*l*(b) ("No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do.").

Maine PUC's claim is that, by approving non-locational transition payments, FERC abandoned the core of the market reform it set out to implement, a mechanism that would "appropriately value capacity resources according to their location." Pet'r Br. 48 (quoting *Devon Power LLC*, 109 FERC ¶ 61,154 at 61,631 (2004)). But the Forward Market, which is the ultimate product of the settlement, includes locational pricing.[7] Hence, the settlement does satisfy FERC's initial concern about non-locational pricing. *See* 115 FERC at 62,322 ("The locational feature in the [Forward Market] ... appropriately addresses on a long-term basis issues regarding payments to capacity in constrained regions."); 117 FERC at 61,720 ("In the June 16 Order, we concluded that the [Forward Market] itself appropriately recognizes location."); *see also* 115 FERC at 62,325 (accepting the locational feature of the Forward Market). The fact that the transition period lacks a locational component does not change the fact that the ultimate result of the settlement proceedings is a new market structure that does account for location.

Maine PUC's specific contention is that separate prices are warranted for Maine during the transition period because Maine has a capacity surplus and is export constrained (so that it would experience lower capacity prices in an actual market). It maintains that FERC refused to consider the evidence that it presented to support this contention. But FERC did consider Maine's argument that it should pay lower transition payments because of its capacity surplus. The Commission offered two interrelated reasons for its conclusion that the transition payments should not have a locational component.

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[7] For the Forward Market, capacity is purchased three years in advance, so the full market design, including the locational element, cannot be implemented until 2010.

First, FERC cited record evidence that projected "little to no variability in capacity prices across New England regions for the period covered by the transition mechanism." 115 FERC at 62,322. Second, to the extent that import constraints do exist in other areas of New England, thereby creating a need for additional capacity, FERC noted that Reliability Must-Run agreements had already been approved and would continue during the transition period, with the costs for these contracts paid locally. *Id.*

To be sure, Maine PUC offered some contradictory evidence about capacity price variability, *see, e.g.*, J.A. 1941-47 (Supplemental Affidavit of Thomas D. Austin), but FERC's orders do "not lack substantial evidence simply because petitioners offered some contradictory evidence," *Ariz. Corp. Comm'n v. FERC*, 397 F.3d 952, 954 (D.C. Cir. 2005) (internal quotation marks omitted). FERC was entitled to reject Maine PUC's evidence and to base its conclusion on different evidence in the record. *See, e.g.*, *Elec. Consumers Res. Council*, 407 F.3d at 1236 ("[T]he court defers to the Commission's resolution of factual disputes between expert witnesses."); *see also Fla. Mun. Power Agency*, 315 F.3d at 368.

Maine PUC insists that FERC cannot rely on the rationale that price separation between Maine and the rest of New England was unsupported by the record. Although FERC did rely on this rationale in its initial order, Maine PUC claims that the Commission abandoned it in its order on rehearing. According to Maine PUC, on rehearing FERC refused to consider data presented by the petitioners and instead found that it was irrelevant whether Maine was export constrained. But despite somewhat infelicitous language in its rehearing order, FERC did not abandon the findings and conclusions of its initial order. To the contrary, the rehearing order first discussed both the evidence presented by Maine PUC,

including Dr. Austin's affidavits, and the data and arguments in the record that contradicted this evidence. *See* 117 FERC at 61,722-23; *see also id.* at 61,724 ("The Commission did consider arguments presented in Dr. Austin's affidavits in approving the Settlement Agreement."). FERC's subsequent statement that the "issue of Maine being export-constrained is not the subject of this proceeding," *id.* at 61,724, did not undo all of that previous discussion. Rather, it merely clarified that the question of whether Maine was export constrained was relevant only insofar as it affected FERC's determination of reasonable rates; it was not an independent question before the Commission. *See id.*

Finally, Maine PUC challenges FERC's denial of a motion that it filed on September 8, 2006, following the Commission's initial June 16 order. By that motion, Maine PUC sought to lodge the Department of Energy's National Electric Transmission Congestion Study, which Maine PUC argued supported its claim that the transition payments should be locational. We accord the Commission "broad discretion in fashioning hearing procedures," *Mich. Consol. Gas Co. v. FERC*, 883 F.2d 117, 125 (D.C. Cir. 1989) (quoting *Lyons v. Barrett*, 851 F.2d 406, 410 (D.C. Cir. 1988)), and find no abuse of discretion here. The motion at issue was filed nearly three months after FERC's decision approving the settlement, and FERC acted reasonably in holding that it "would be inappropriate to accept evidence at this extremely late date in this proceeding (after a dispositive order has been issued), since it would effectively deny parties the opportunity to respond to the evidence." 117 FERC at 61,724. FERC similarly denied untimely motions to intervene by Bridgeport Energy, LLC and Casco Bay Energy Company, LLC, which had been filed several weeks before Maine PUC's motion. *See id.* at 61,715.

Accordingly, we reject all of Maine PUC's attacks on FERC's decision to accept non-locational pricing during the transition period.

IV.

Section 4.C of the settlement agreement provides that the transition payments and the final prices from the Forward Market auctions will be reviewed under the "public interest" standard rather than the "just and reasonable" standard. 115 FERC at 62,333. This is more than a matter of semantics: the public interest standard is "much more restrictive" than the just and reasonable standard, which means that the settlement agreement makes it harder to successfully challenge the transition payments and Forward Market auction prices. *Wisc. Pub. Power, Inc. v. FERC*, 493 F.3d 239, 271 (D.C.Cir. 2007) (citation omitted). The agreement states that the public interest standard will apply to all future challenges to the transition payments and final auction prices "whether the change is proposed by a Settling Party, a non-Settling Party, or the FERC acting *sua sponte*." 115 FERC at 62,333. Petitioners—who were not parties to the settlement agreement—assert that this provision will deprive them of their statutory right to challenge rates under the "just and reasonable" standard. We agree, and we grant the petition for review on this issue.

* * *

Under the *Mobile-Sierra* doctrine, "FERC may abrogate or modify freely negotiated private contracts that set firm rates or establish a specific methodology for setting the rates for service . . . only if required by the public interest." *Atl. City Elec. Co. v. FERC*, 295 F.3d 1, 14 (D.C. Cir. 2002). This doctrine recognizes the superior efficiency of private bargaining, and its purpose is "to subordinate the statutory filing mechanism to the broad and familiar dictates of contract law." *Borough of Lansdale v. FPC*, 494 F.2d 1104, 1113 (D.C. Cir. 1974).

Thus, when the parties to a rate dispute reach a contractual settlement, FERC must enforce the terms of the bargain unless the public interest requires otherwise—that is, unless the negotiated rates "might impair the financial ability of the public utility to continue its service, cast upon other customers an excessive burden, or be unduly discriminatory." *FPC v. Sierra Pac. Power Co.*, 350 U.S. 348, 355, 76 S. Ct. 368, 100 L. Ed. 388 (1956). In the instant case, we are presented with a question of first impression: may the Commission approve a settlement agreement that applies the highly-deferential "public interest" standard to rate challenges brought by non-contracting third parties? We think not.

Section 206 of the Federal Power Act provides: "Whenever the Commission, after a hearing had upon its own motion or upon complaint, shall find that any rate, charge, or classification . . . is unjust, unreasonable, unduly discriminatory or preferential, the Commission shall determine the just and reasonable rate . . . and shall fix the same by order." 16 U.S.C. § 824e(a). In other words, when a party files a complaint against a rate or charge, FERC must adjudicate the challenge under the "just and reasonable" standard. The *Mobile-Sierra* doctrine carves out an exception to this rule based on the "familiar dictates of contract law." *Lansdale*, 494 F.2d at 1113. When two or more parties reach a negotiated settlement over a disputed rate, FERC applies a strong presumption that the settled rate is just and reasonable, and the Commission may only set aside the contract for the most compelling reasons.[8] The purpose of the *Mobile-Sierra*

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[8] As one commentator has noted, the *Mobile-Sierra* doctrine "recognize[s] that the existence of a contract infuses the rate with the attribute of reasonableness . . . ." Carmen L. Gentile, *The* Mobile-Sierra Rule: *Its Illustrious Past and Uncertain Future*, 21 ENERGY L.J. 353, 357 (2000).

doctrine is "to preserve the benefits of the parties' bargain as reflected in the contract, assuming that there was no reason to question what transpired at the contract formation stage." *Atl. City*, 295 F.3d at 14. For example, in the *Sierra* case, Pacific Gas & Electric (PG&E) had surplus hydroelectric power, which it sold to Sierra Pacific Power Company at a very low rate. 350 U.S. at 351-52, 76 S. Ct. 368. When the surplus power was no longer available, PG&E—with the Commission's approval—reneged on its contract and increased Sierra's rates. *Id.* at 352, 76 S. Ct. 368. The Supreme Court held for Sierra, stating that "neither PG&E's filing of the new rate nor the Commission's finding that the new rate was not unlawful was effective to change PG&E's contract with Sierra." *Id.* at 353, 76 S. Ct. 368. The Court required the Commission to apply the highly-deferential "public interest" standard of review to challenges to contractually-established rates, in order to preserve the terms of the parties' bargain. *Id.* at 355, 76 S. Ct. 368; *see also Lansdale*, 494 F.2d at 1107-14 (holding that FERC may not approve a utility's breach of a settled rate contract unless the contract rates "contravened the public interest").

Courts have rarely mentioned the *Mobile-Sierra* doctrine without reiterating that it is premised on the existence of a voluntary contract between the parties. In *Mobile*, the Supreme Court stated that "the relations *between the parties*" may be established by contract, subject only to "public interest" review. *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332, 339, 76 S. Ct. 373, 100 L. Ed. 373 (1956) (emphasis added). Similarly, this Court has emphasized that the deferential public interest standard only applies to "*freely negotiated private contracts* that set firm rates or establish a specific methodology for setting the rates for service." *Atl. City*, 295 F.3d at 14 (emphasis added); *see also Maine*

PUC v. FERC, 454 F.3d 278, 283-84 (D.C. Cir. 2006); *Richmond Power & Light v. FPC*, 481 F.2d 490, 493 (D.C. Cir. 1973) ("The contract between the parties governs the legality of the filing.").

This case is clearly outside the scope of the *Mobile-Sierra* doctrine. As we explained, *Mobile-Sierra* is invoked when "one party to a rate contract on file with FERC attempts to effect a unilateral rate change by asking FERC to relieve its obligations under a contract whose terms are no longer favorable to that party." *Maine PUC*, 454 F.3d at 284. Here, the settling parties are attempting to thrust the "public interest" standard of review upon non-settling third parties who have vociferously objected to the terms of the settlement agreement. As the Supreme Court has noted, "[i]t goes without saying that a contract cannot bind a nonparty." *EEOC v. Waffle House, Inc.*, 534 U.S. 279, 294, 122 S. Ct. 754, 151 L. Ed. 2d 755 (2002). The *Mobile-Sierra* doctrine applies a more deferential standard of review to preserve the terms of the bargain as between the contracting parties. *Atl. City*, 295 F.3d at 14. But when a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply; the proper standard of review remains the "just and reasonable" standard in section 206 of the Federal Power Act.

In defense of the *Mobile-Sierra* provision, FERC argues that the "public interest" standard will only apply to future challenges to a narrow category of rates: the transition payments and the final auction clearing prices from the Forward Market. 115 FERC at 62,335. This is not persuasive. It is equivalent to arguing that FERC will use an illegal standard sparingly. Despite the "limited" applicability of the public interest standard, FERC's approval of this agreement still deprives non-settling parties of their statutory right to have rate challenges adjudicated under the "just and reasonable" standard.

And in any event, we are skeptical of FERC's characterization of the *Mobile-Sierra* provision as "narrow" or "limited." As petitioners' counsel noted at oral argument, if circumstances change after a rate has initially been approved by the Commission, then (under the settlement agreement) subsequent challenges to that rate would be reviewed under the public interest standard. Recording of Oral Arg. at 29:25-31:20. The *Mobile-Sierra* provision thus departs from the usual "just and reasonable" standard and makes it harder for petitioners to successfully challenge rates in cases of changed circumstances.[9]

FERC also argues that in other recent cases, the Commission has approved contracts that apply the "public interest" standard to non-contracting third parties. 117 FERC at 61,727 n.103. This may show that the Commission's policy has been consistent—although even FERC concedes that is so only since 2002—but it does not necessarily support the policy's legality, since none of the cited orders have been subject to judicial review on the *Mobile-Sierra* issue. FERC states that "there is no Commission or court precedent that supports a finding that a non-signatory may unilaterally seek changes to a *Mobile-Sierra* 'public interest' contract under the 'just and reasonable' standard of review." 115 FERC at 62,335 (citation omitted). It could just as easily be said that there is no "court precedent" that supports altering third parties' statutory rights based on a contract that they refused to sign. Moreover, while FERC can find no "precedent" in support of petitioners' arguments, the

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[9] FERC asserts that third parties' interests are adequately safeguarded because under *Mobile-Sierra*, the Commission "retains significant authority to protect non-parties to the settlement from harm." 115 FERC at 62,335. But whatever comfort third parties might derive from FERC's continued ability to defend their interests, the existence of such powers does not justify derogation of the statutory right to "just and reasonable" review of rates.

relevant statutory language is quite clear: section 206 of the FPA states that "upon complaint" the Commission must determine whether the challenged rate is "unjust, unreasonable, unduly discriminatory or preferential." 16 U.S.C. § 824e(a). Lastly, FERC argues that the *Mobile-Sierra* provision is necessary to promote price certainty and contract stability. As explained above, the *Mobile-Sierra* doctrine is designed to ensure contract stability *as between the contracting parties—i.e.*, to make it more difficult for either party to shirk its contractual obligations. *Atl. City*, 295 F.3d at 14. It makes no sense to say that the values of "stability" and "certainty" are furthered by applying the deferential standard of review to the eight parties that *refused* to agree to the terms of the settlement.

V.

Petitioners also contend that FERC's approval of the Forward Market exceeds the Commission's jurisdiction because it forces utilities to purchase a specific amount of capacity. Petitioners assert that FERC lacks jurisdiction under the Federal Power Act, which provides that the Commission "shall not have jurisdiction . . . over facilities used for the generation of electric energy." 16 U.S.C. § 824(b)(1). In response, FERC argues that the settlement agreement only addresses prices, which are unquestionably within FERC's jurisdiction. The Commission's interpretation of the scope of its jurisdiction is entitled to *Chevron* deference. *Okla. Natural Gas Co. v. FERC*, 28 F.3d 1281, 1283-84 (D.C. Cir. 1994).

We agree with the Commission that the Forward Market itself does not exceed FERC's jurisdiction. The Federal Power Act grants the Commission broad authority over "the sale of electric energy at wholesale in interstate commerce." 16 U.S.C. § 824(b)(1). The protracted litigation over Must-Run agreements, the locational installed capacity market, and the Forward Market

is fundamentally a dispute over the *rates* that will be paid to suppliers of capacity. The two key components of the settlement agreement—the transition payments and the Forward Market auctions—"establish a mechanism and market structure for the *purchase and sale* of installed capacity at wholesale ... [and] determine the *prices* for those sales." 115 FERC at 62,339 (emphasis added). Of course, it is a basic principle of economics that prices affect supply—the auction clearing prices in each subregion of New England will certainly influence the amount of capacity that generators are willing to supply. Indeed, one of the primary purposes of the new market mechanism is to "provide[ ] incentives to attract new infrastructure where needed." *Id.* at 62,316. But an incentive is not a mandate. The mere fact that the Forward Market will encourage new supply does not mean that it *regulates* "facilities used for the generation of electric energy." 16 U.S.C. § 824(b)(1). Rather, the Forward Market is designed to address pricing issues, which fall comfortably within FERC's statutory authority over "the sale of electric energy at wholesale in interstate commerce." *Id.* We have previously held that the Commission has jurisdiction over a "deficiency charge" that was imposed upon transmission providers who failed to procure a specified amount of capacity:

> The deficiency charge ... must be deemed to be within the Commission's jurisdiction because it [ ] represents a charge for the power and service the overloaded participant receives—or it is at least a rule or practice affecting the charge for these services.

Municipalities of Groton v. FERC, 587 F.2d 1296, 1302 (D.C. Cir. 1978).

In support of their jurisdictional argument, petitioners focus heavily upon the "installed capacity requirement," which is "the total amount of capacity required by the

system to meet peak load plus a reserve margin." 115 FERC at 62,338-39 n.177. This requirement ensures that transmission providers have procured enough capacity to maintain the reliability of the grid. Under the settlement agreement, transmission providers must purchase at least enough capacity in the annual auctions to meet their installed capacity requirements. *Id.* at 62,307. The Forward Market simply takes the capacity requirement as a given and uses it as an input into the auction mechanism. As FERC explained, "[the Forward Market] only establishes a market design for determining capacity charges; it does not alter [the capacity requirement] or in any way determine the appropriate amount of capacity that must be available." 117 FERC at 61,730. Rather, the capacity requirement is computed by ISO-New England in conjunction with a regional standard-setting body. 115 FERC at 62,338-39 n.177. To be sure, the methodology for calculating the installed capacity requirement is part of the ISO's tariff, and must be filed with the Commission for approval. *See ISO New England, Inc.*, 120 FERC ¶ 61,234 at 61,974-75 (2007). To the extent petitioners believe they are aggrieved by the ISO's installed capacity requirement, and more specifically, FERC's approval of that requirement on jurisdictional grounds, they may challenge that agency action. In fact, petitioners have already filed such a suit. *Conn. Dep't of Public Util. Control v. FERC*, No. 07-1375 (D.C. Cir. filed Sept. 19, 2007). But the Forward Market does not exceed FERC's jurisdiction merely because it incorporates the exogenously-determined installed capacity requirement into the auction mechanism. We thus deny the petition for review with respect to the jurisdictional issue.

VI.

For the aforementioned reasons, the consolidated petitions for review are granted with respect to the *Mobile-Sierra* issue, denied with respect to all other

issues, and remanded to the Commission for further proceedings.

So ordered.

APPENDIX B

UNITED STATES OF AMERICA FEDERAL ENERGY REGULATORY COMMISSION

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117 FERC ¶ 61,133

Before Commissioners: Joseph T. Kelliher, Chairman; Suedeen G. Kelly, Marc Spitzer, Philip D. Moeller, and Jon Wellinghoff

Devon Power LLC Docket No. ER03-563-060

ORDER ON REHEARING AND CLARIFICATION

(Issued October 31, 2006)

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1. In these proceedings, the Commission has been addressing a proposal by ISO New England, Inc. (ISO-NE) to establish a locational installed capacity (LICAP) mechanism. That proposal was made in response to Commission orders identifying flaws in New England's current capacity market, and was further developed through subsequent hearing procedures. As this proceeding has developed, additional evidence has been produced regarding the flaws in the current capacity market and the resulting impacts those flaws have had on New England's electric system infrastructure. As discussed in more detail below, the Commission established additional procedures to consider how the LICAP mechanism would address the deficiencies in the current capacity market and meet New England's projected need for new infrastructure in coming years. Those additional procedures

also gave the parties an opportunity to discuss and develop potential alternatives to the LICAP mechanism.

2. On March 6, 2006, a broad group of the parties to this proceeding (collectively Settling Parties[1]) filed a proposed settlement (Settlement Agreement) that would resolve all issues in this matter. The Settlement Agreement contained an alternative to LICAP, called the Forward Capacity Market (FCM). The settlement was contested. In a June 16, 2006 Order,[2] we accepted the proposed Settlement Agreement, finding that as a package, it presents a just and reasonable outcome for this proceeding consistent with the public interest.

3. In this order, the Commission addresses requests for rehearing and clarification of the June 16 Order. As discussed in more detail below, the Commission will deny rehearing, and clarify that ISO-NE should model export constraints in the auction, consistent with the Settlement Agreement.

I. Background

A. Prior Proceedings

4. The Initial Decision contains a detailed history of this proceeding up to the point of its issuance, which will not be repeated here except as needed for clarity.[3] The June 16 Order also recounts certain key points in the prior proceedings.[4]

5. These proceedings began in response to the February 26, 2003 filing by Devon Power LLC, Middletown Power

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[1] Settling Parties are identified in Appendix A to this order.

[2] *Devon Power LLC*, 115 ¶ 61,340 (2006) (June 16 Order).

[3] *See Devon Power LLC*, 111 FERC ¶ 63,063 at P 2-36 (2005) (Initial Decision).

[4] *See* June 16 Order at P 3-14.

LLC, Montville Power LLC, Norwalk Power LLC and NRG Power Marketing Inc. (collectively NRG) of four cost-of-service reliability-must-run (RMR) agreements covering 1,728 megawatts of generating capacity located within Connecticut and the constrained Southwest Connecticut area. In a series of orders addressing NRG's filing[5] as well as RMR agreements filed by other entities,[6] the Commission rejected the majority of the RMR agreements, out of concern about the effect of widespread use of such contracts could have on the competitive market. The Commission stated that ISO-NE, "rather than focusing on and using stand-alone RMR agreements, should incorporate the effect of those agreements into a market-type mechanism."[7] As a long-term solution to problems in the capacity market creating the need for RMR agreements, the Commission directed ISO-NE to file by March 1, 2004, for implementation by June 1, 2004, "a mechanism that implements location or deliverability requirements in the [installed capacity (ICAP)] or resource adequacy market . . . so that capacity within [designated congestion areas] may be appropriately compensated for reliability."[8]

6. On March 1, 2004, ISO-NE made its filing in compliance with the April 25 Order. In the compliance filing, ISO-NE proposed a LICAP mechanism that would add a locational element to the current ICAP market, establishing four ICAP regions with separate ICAP require-

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[5] *Devon Power LLC*, 102 FERC ¶ 61,314 (2003) (March 25 Order); *Devon Power LLC*, 103 FERC ¶ 61,082 (2003) (April 25 Order); *Devon Power Company*, 104 FERC ¶ 61,123 (July 24 Order).

[6] *PPL Wallingford Energy LLC*, 103 FERC ¶ 61,185 (2003); *PPL Wallingford Energy LLC*, 105 FERC ¶ 61, 324 (2003).

[7] *See* April 25 Order at P 29.

[8] *Id.* at P 37.

ments: Maine, Connecticut, Northeast Massachusetts/ Boston (NEMA/Boston), and the remainder of New England (Rest of Pool). Under the proposal, capacity transfer limits would be established to limit the amount of ICAP that load serving entities in one region could purchase from another region. Additionally, ISO-NE proposed to use a downward sloping demand curve to establish the amount of ICAP that must be procured and the price for that capacity. Additionally, under the proposed LICAP mechanism, capacity transfer rights would be allocated to load or generators, depending on their location, to allow market participants to hedge against congestion costs. Under the proposal, holders of capacity transfer rights between two ICAP regions would receive the difference in ICAP prices between those regions.

7. In a June 2, 2004 Order,[9] the Commission established hearing procedures regarding ISO-NE's compliance filing, and delayed the implementation of the LICAP mechanism from the proposed June 1, 2004 date until January 1, 2006. The Commission stated that it agreed with two broad concepts in ISO-NE's proposal. First, the Commission found it appropriate to establish separate ICAP regions, but questioned whether the regions proposed by ISO-NE adequately reflected where infrastructure investment is needed most, specifically noting the constrained area of Southwest Connecticut. Second, the Commission agreed with the overarching concept of a demand curve, but found that more information was necessary to develop appropriate parameters for the curve. As a result of these findings, the Commission directed ISO-NE to submit a further filing addressing whether the Commission should revise the LICAP proposal to create a separate ICAP region for Southwest Connecticut.

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[9] *Devon Power LLC*, 107 FERC ¶ 61,240 (2004) (June 2 Order).

Additionally, the Commission established a separate investigation and paper hearing in Docket No. EL04-102-000 to determine whether a separate energy load zone should be created for Southwest Connecticut, and whether it should be implemented in advance of LICAP. Finally, the Commission established hearing procedures to determine the appropriate demand curve parameters, the proper method for calculating capacity transfer limits, the appropriate method for determining the amount of capacity transfer rights to be allocated, and the proper allocation of capacity transfer rights. In subsequent orders, the Commission addressed ISO-NE's filing regarding the creation of a separate ICAP region for Southwest Connecticut, and denied rehearing and granted clarification in part of the June 2 Order.[10]

8. On June 15, 2005, the Presiding Judge issued an Initial Decision on the issues set for hearing in the June 2 Order.[11] The Initial Decision largely (with some variation) adopted the demand curve proposed by ISO-NE in its August 31, 2004 initial testimony, and also ruled on the appropriate allocation of capacity transfer rights and the appropriate methodology for calculating capacity transfer limits. Briefs on Exceptions to the Initial Decision were filed on July 15, 2005, and Briefs Opposing Exceptions were filed on August 4, 2005.

9. In section 1236 of the Energy Policy Act of 2005, signed into law on August 8, 2005, Congress noted the

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[10] *See* June 2 Order, *order on reh'g and clarification*, *Devon Power LLC*, 109 FERC ¶ 61,154 (2004), *reh'g denied*, 1001 FERC ¶ 61,315 (2005); *see also Devon Power LLC*, 109 FERC ¶ 61, 156 (2004) (order on compliance filing directing establishment of Southwest Connecticut region), *order on reh'g and clarification*, 110 FERC ¶ 61,313 (2005).

[11] *See supra* note 3.

New England Governors' concerns that the LICAP proposal would not provide adequate capacity or reliability while imposing high costs on consumers.[12] Congress declared that the Commission should carefully consider the states' objections.

10. Several entities (mostly state entities and load representatives) requested oral argument before the Commission on the exceptions to the Initial Decision, pursuant to Rule 711(c) of the Commission's Rules of Practice and Procedure.[13] In an August 10, 2005 Order, the Commission granted these requests and scheduled oral argument for September 20, 2005.[14] Additionally, the Commission stated that, in light of its decision to hear oral arguments, "we have determined that the implementation of the LICAP mechanism, if it proceeds, will not be earlier than October 1, 2006."[15]

11. The oral argument focused on whether the LICAP mechanism, as adopted in the Initial Decision, or any alternative approach would provide for just and reasonable wholesale power prices in New England, at levels that encourage needed generation additions and whether LICAP or any alternative approach would provide adequate assurance that necessary electric generation capacity or reliability will be provided. The Commission also asked the parties to address at oral argument what are the costs, benefits, and economic impacts of the proposal (or any alternative approach), compared to continued reliance on the status quo, such as the cost of RMR agreements. Both at the oral argument and in briefs

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[12] Pub. L. No. 109-58 § 1236, 119 Stat. 961 (2005).

[13] 18 C.F.R. § 385.711(c) (2005).

[14] *Devon Power LLC*, 113 FERC ¶ 61,075 (2005).

[15] *Id.* at P 5.

filed prior to the oral argument, parties to the proceeding were given the opportunity to present alternatives to LICAP directly to the Commission.[16] Parties presented two alternatives to LICAP in their briefs and at oral argument: the New England Resource Adequacy Market and the New England Locational Resource Adequacy Market.

12. Following the oral argument, the Commission issued an order giving the parties an additional opportunity to pursue a settlement on an alternative to the LICAP mechanism.[17] In that order, the Commission stated that it remained concerned about the resource adequacy situation in New England (particularly in the congested areas of Southwest Connecticut and Northeastern Massachusetts), noting that "[t]he parties at the oral argument generally agreed that the status quo is failing and that generation resources are not being added at a rate necessary to maintain reliability and assure just and reasonable wholesale power prices."[18] The Commission directed the Chief Administrative Law Judge to appoint a settlement judge to guide the process of developing a proposed alternative to LICAP. Additionally, the Commission stated that it would continue to evaluate the Initial Decision, and directed ISO-NE to make a compliance filing to aid in its consideration of the Initial Decision.[19]

B. Settlement Agreement

13. On March 6, 2006, Settling Parties filed the Settlement Agreement, which they stated would resolve all is-

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[16] *See* Notice Scheduling Oral Argument, Docket No. ER03-563-030 (August 25, 2005).

[17] *Devon Power LLC*, 113 FERC ¶ 61,075 (2005) (October 21 Order).

[18] *Id.* at P 5.

[19] *Id.* at P 10-14.

sues in this matter. The Settlement Agreement introduces the FCM, which is an alternative to LICAP. In general, when fully implemented, the FCM will establish annual auctions for capacity. These auctions will procure capacity three-plus years in advance of the commitment period.[20] The first FCM auction will be held in the first quarter of 2008 for the commitment period of June 1, 2010 to May 31, 2011. The initial auction for the commitment period beginning June 1, 2011 will be held shortly thereafter. The Settlement Agreement also contains a transition period prior to the first commitment period of this FCM. During this transition period—which begins December 1, 2006 and ends June 1, 2010—fixed payments will be made to all installed capacity resources. The Settling Parties asked that the Commission consider the Settlement Agreement as a package under the approaches outlined in *Trailblazer Pipeline Company*.[21] Further details concerning the Settlement Agreement and the design of the FCM and the transition period are included in our discussion below where relevant, and can also be found in the June 16 Order at P 15-37.

C. June 16 Order

14. In the June 16 Order, the Commission accepted the Settlement Agreement, concluding that as a package, it presented a just and reasonable outcome that is consistent with the public interest. Specifically, the Commission first found that under the standards announced in *Trailblazer*, the Settlement Agreement is consistent with the public interest.[22] Second, the Commission found that

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[20] The first auction will be held less than three years in advance, due to the software implementation schedule.

[21] 85 FERC ¶ 61,345 (1998), *order on reh'g*, 87 FERC ¶ 61,110 (1999) (*Trailblazer*).

[22] June 16 Order at P 62-67.

the overall result of the Settlement Agreement, considered as a package, is just and reasonable. To make this finding, the Commission utilized the second approach of *Trailblazer*, and concluded "that the parties objecting to the Settlement Agreement would "be in no worse position under the terms of the settlement than if the case were litigated," and that the Settlement Agreement, as a package, achieves an overall just and reasonable result within a zone of reasonableness.[23] The Commission also analyzed specific issues raised in comments and protests, including issues regarding the transition mechanism and the design of the FCM itself. These portions of the June 16 Order are discussed below where relevant to the requests for rehearing and/or clarification.

II. Discussion

A. Procedural Matters

15. Requests for rehearing were filed by The Industrial Energy Consumers Group (IECG), Maine Public Utilities Commission and Maine Public Advocate (Maine Parties), and Objecting Parties.[24] Maine Parties also filed a motion for clarification.

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[23] *Id.* at P 70, *citing Trailblazer*, 87 FERC ¶ 61,110 at 61,339. The four approaches laid out in *Trailblazer* are: (1) Commission renders a binding merits decision on each contested issue, (2) Commission approves the settlement based on a finding that the overall settlement as a package is just and reasonable, (3) Commission determines that the benefits of the settlement outweigh the nature of the objections, and the interests of the contesting party are too attenuated, and (4) Commission approves the settlement as uncontested for the consenting parties, and severs the contesting parties to allow them to litigate the issues raised.

[24] The Objecting Parties are the Attorney General of the Commonwealth of Massachusetts; Richard Blumenthal, Attorney General for the State of Connecticut; Massachusetts Department of Telecommu-

16. Motions to answer and answers were filed by ISO-NE, the New England Power Pool Participants Committee (NEPOOL), and the Connecticut Department of Public Utility Control (CT DPUC). Rule 213(a)(2) of the Commission's Rules of Practice and Procedure[25] prohibits an answer to a request for rehearing unless otherwise ordered by the decisional authority. We will accept the answers of ISO-NE, NEPOOL and CT DPUC because they have provided information that assisted us in our decision-making process.

17. On August 9, 2006, motions to intervene out-of-time were filed by Bridgeport Energy, LLC and Casco Bay Energy Company, LLC. When late intervention is sought after the issuance of a dispositive order, the prejudice to other parties and burden upon the Commission of granting the late intervention may be substantial. Thus, movants bear a higher burden to demonstrate good cause for granting such late intervention.[26] Bridgeport Energy and Casco Bay have not met this higher burden of justifying their late intervention, and, therefore, their late intervention is denied.

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nications and Energy; The Energy Consortium; the NEPOOL Industrial Customer Coalition; and NSTAR Electric & Gas Corporation. The Massachusetts Department of Telecommunications and Energy was not a party to the comments of the Objecting Parties filed March 27 and April 5, 2006 in response to the Settlement Agreement.

[25] 18 C.F.R. § 385.213(a)(2) (2006).

[26] *See, e.g., Midwest Independent Transmission System Operator, Inc.*, 102 FERC ¶ 61,250 at P 7 (2003).

B. Requests for Rehearing and/or Clarification and Commission Conclusions

1. Application of *Trailblazer* Standards, Sufficiency of Record Evidence, and Transition Period

18. In the June 16 Order, the Commission followed the *Trailblazer* precedent. In particular, the Commission first found that the Settlement Agreement is consistent with the public interest, noting that it resolves the deficiencies in New England's existing capacity market previously identified by the Commission, and provides necessary solutions to resolve the resulting impacts those deficiencies have had on New England's infrastructure.[27] To address the contested issues raised by the parties, the Commission employed the second approach of *Trailblazer*; under that approach, even if some individual aspects of a settlement may not be just and reasonable standing alone, the Commission may approve a contested settlement as a package if the overall result of the settlement is just and reasonable. The Commission found that the overall result of the Settlement Agreement is just and reasonable, for many of the same reasons that it found that the settlement is in the public interest.[28] Also, as required by the *Trailblazer* precedent, the Commission concluded that the parties opposing the Settlement Agreement would be no worse off under the settlement than through continued litigation.[29] The Commission went on to address the contested issues to ensure the overall justness and reasonableness of the settlement as a package.

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[27] June 16 Order at P 62-67.

[28] *Id.* at P 71.

[29] *Id.* at P 72.

19. Additionally, between December 1, 2006 and the beginning of the first FCM period (June 1, 2010), the Settlement Agreement provides for a transition period, during which fixed payments will be made to all installed capacity. Transition payments will be netted against RMR payments and will be considered capacity payments for the purposes of netting in the locational forward reserves market. Transition payments will be adjusted to account for unit availability. During the three and one-half year transition period, transition payments will be adjusted downward according to a modified equivalent demand forced outage rate (EFORd) measurement, which most heavily weights availability during times of greatest need.

20. In the June 16 Order, the Commission found that, while it may not consider the transition payments ideal as a single market design element, when considered as part of the larger Settlement Agreement (consistent with the second approach of *Trailblazer*), they serve as a reasonable transitory mechanism that enables the New England region to shift to the FCM. The Commission based this finding on several aspects of the transition payments. First, based on record evidence from the hearing, the transition payments fall within the reasonable range of capacity prices, and contesting parties are in no worse position under the Settlement Agreement than they would have been through continued litigation. Second, the transition payments, in the first years, are less than the cost of new entry. Third, the transition payments result in just and reasonable rates for existing generators.

Requests for Rehearing

21. IECG argues that the Commission may apply one of the four *Trailblazer* approaches only if the record contains substantial evidence that the proposal establishes

just and reasonable rates. IECG argues, however, that there is no substantial record evidence that the Settlement Agreement produces just and reasonable rates for the services rendered and thus the Commission may not apply a *Trailblazer* approach. IECG argues that the Commission provides no reasoning or analysis to support its conclusion that substantial record evidence exists. Maine Parties assert that the record is insufficient to support approval of the proposed settlement and thus, under *Trailblazer*, the Commission cannot conclude that Maine Parties will be better off under the settlement than if the case were litigated.

22. With regard to the transition mechanism in particular, IECG contends that the evidence in the record has nothing to do with the market design, structure or product to be paid for during the transition period. IECG asserts that, unlike the product contemplated under the LICAP proposal, the transition payments have no locational component, perpetuate RMR agreements, will not provide an incentive for new entry and will not be adjusted for surplus or scarcity. IECG states that nothing in the record evidence supports transition payments as anything more than a cheaper option than LICAP payments, and argues that cheaper is insufficient to satisfy the just and reasonable standard. Maine Parties assert that the Commission cannot measure the transition payments against the projected cost of a proposal that was never adjudicated by the Commission.

23. IECG contends that there is no formula that justifies the transition rates. IECG asserts that it is the Settling Parties' obligation to demonstrate that there is a "rational methodology for determining a range of reasonableness for the particular product being priced and that the particular rates set by the Settlement fall within it or

may be derived by reference to it."[30] IECG argues that the Commission presents no methodology or evidence to support its assertion that "the transition payments are reasonable rates for existing generators until the FCM begins."[31] IECG argues that this assertion is not evidence, and the Commission cannot point to record evidence, that the transition payments fall within any range of reasonableness established by any methodology.

24. Maine Parties argue that comparing transition payments to LICAP rates because they had been accepted in an Initial Decision does not meet the *Trailblazer* standard. Maine Parties argue that reliance on LICAP rates as the likely outcome of litigation or setting the parameters of the range of reasonableness must be based on more than the administrative law judge's recommendation to adopt the proposal. Maine Parties state that there has not been an adjudication of all the underlying assumptions, factual determinations and conclusions of law embodied in the initial decision. Maine Parties assert that it is unreasonable and arbitrary to use load parties' demand curve proposals[32] to determine that the transition payments fall within the range of reasonableness, given that the Settlement Agreement does not include a demand curve. Maine Parties also contend that the transition payments approved in the FCM Order ignore location and thus cannot be reconciled with previous Commission determinations that it is essential to value capacity by location.

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[30] IECG Request for Rehearing at 11.

[31] June 16 Order at P 102.

[32] Maine Parties note that while several load parties proposed demand curves, they did so under objection, as the scope of the hearing did not include the presentation of alternative mechanisms.

25. Objecting Parties assert that the Commission erred in approving transition payments that have no legitimate regulatory purpose. Objecting Parties assert that, in the June 2 Order on the ISO's March 1 Filing, the Commission rejected transition payments proposed by ISO-NE, on the basis that they were out-of-market arrangements.

26. Objecting Parties argue that no demand curve parameters were evaluated and ruled on by the Commission. Objecting Parties further argue that the Commission never determined that the demand curves used for price projections may be just and reasonable. Objecting Parties assert that the particular demand curves selected by the Commission to establish a range of price projections skew the determination of justness and reasonableness. Objecting Parties contend that to the extent another demand curve, other than ISO-NE's, was selected to establish the range of price projections, a different result would emerge.

27. Finally, Objecting Parties argue that transition payments are "pure largesse" to gain supplier sign-on to the Settlement Agreement.[33] Objecting Parties assert that generators that actually require additional financial support for reliability services have negotiated RMR agreements with ISO-NE. Objecting Parties assert further that certain suppliers that are currently recovering costs (without transition payments) will receive transition payments while avoiding having to demonstrate that they are needed for reliability purposes or are not recovering costs in the energy market. Objecting Parties conclude that the Settlement Agreement is an expensive compromise for New England consumers and that the Commission's rationale for approval of the transition payments

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[33] Request for Rehearing of Objecting Parties at 18.

fails to comply with the Commission's statutory mandate to protect the public interest from unjust and unreasonable rates.

Answers

28. In response to IECG's arguments that the transition payments cannot be compared to the LICAP capacity product, ISO-NE states that, whether purchased under LICAP or FCM, firm capacity is still capacity capable of producing energy when needed. ISO-NE asserts that the means of determining the price differs under each market design but does not alter the nature of the product itself. Additionally, it contends that the Commission correctly found that the transition payments are within the zone of reasonableness. ISO-NE states that reliance on the Maine/Vermont and ISO demand curves to provide a narrow range of rates that provide a reasonable basis for comparison to the transition payments is appropriate. ISO-NE argues that the Commission is entitled to apply its expertise to the extensive record before it, and to draw conclusions about the result the record would support with respect to transition pricing. ISO-NE concludes by asserting that the Commission's finding regarding the transition payments is supported by comparison to the cost of doing nothing. ISO-NE notes that the price of capacity has increased, with the deficiency charge clearing at $2.50/kW-month in the June ICAP auction and that "it is only a matter of time" before the prices in the capacity market hit the $6.66/kW-month cap, thus further supporting the transition charge both as to level and existence.[34]

29. The CT DPUC states that parties to the hearing developed an extensive record surrounding the estimated

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[34] Answer of ISO-NE at 11-12.

benchmark cost of capacity (EBCC), which was intended to reflect the competitive cost of new entry for generating capacity over the long term. Thus, the CT DPUC asserts that the record contains substantial evidence establishing costs for generation capacity resources across New England. CT DPUC further argues that there has been broad agreement that the long-term cost of new entry reflects a reasonable capacity payment. The CT DPUC notes that numerous parties—ISO-NE, load representatives, generators, Commission Staff—provided analysis regarding the EBCC. The CT DPUC argues that using the lowest long-term cost of new entry[35] with a high peak energy rent (PER) offset[36], the record fully supports the finding that transition payments plus peak energy rents are less than the cost of new entry.

Commission Conclusion

30. The Commission denies these requests for rehearing. The June 16 Order addressed the Settlement Agreement in a manner fully consistent with the Commission's *Trailblazer* precedent, and employed relevant and substantial record evidence to determine that the Settlement Agreement achieves an overall just and reasonable result.

31. We reiterate the discussion in the June 16 Order that the Commission has broad authority and discretion under Rule 602(h) of its regulations to address contested settlements.[37] Courts have confirmed the Commission's authority to approve contested settlements, so long as the

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[35] The EBCC applicable to Maine was $7.27 per kW-month.

[36] The CT DPUC argues that the Commission may use PER values of $0.58, $0.60, $0.83, $1.00 for the years 2006-2010.

[37] 18 C.F.R. § 385.602(h) (2006).

proposal will establish just and reasonable rates.[38] Under Rule 602(h), the Commission may decide the merits of the contested issues if the record contains substantial evidence on which to base a reasoned decision or if the Commission determines that there is no genuine issue of material fact. If the Commission finds that the record lacks substantial evidence or that the contesting parties or issues cannot be severed, the Commission may establish hearing procedures to supplement the record, or it may take other appropriate action.[39]

32. In *Trailblazer*, the Commission explained and amplified its approach to addressing contested settlements under the broad authority and discretion described in Rule 602(h). In *Trailblazer*, the Commission explained four approaches it has taken for approving a contested settlement despite the objections of the contesting party. Under the first approach, if there is an adequate record, the Commission can address each of the contested issues on the merits, approving the settlement if the Commission finds that each of the contesting party's contentions lacks merit. This approach is appropriate where the issues are primarily policy issues or the parties have agreed that the record is sufficient to decide the issues on the merits.

33. However, as the Commission explained in *Trailblazer* and reiterated in the June 16 Order that, even

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[38] *See New Orleans Public Service, Inc. v. FERC*, 659 F.2d 509, 511-12 (5th Cir. 1981), *citing Placid Oil Co. v. FPC*, 483 F.2d 880, 893 (5th Cir. 1973), *aff'd sub nom. Mobil Oil Corp. v. FPC*, 417 U.S. 283, 312-13 (1974).

[39] *See* 18 C.F.R. § 385.602(h)(1)(ii)(B) (2005). In *Arctic Slope Regional Corp. v. FERC*, 832 F.2d 158, 164 (D.C. Cir. 1987), the court observed that "the breadth of discretion trumpeted by Rule 602(h)(1)(ii)(B) is manifest."

where the settlement cannot be approved under the first approach, it may be approved under other approaches. Thus, under the second approach, even if some individual aspects of a settlement may not be just and reasonable standing alone, the Commission may approve a contested settlement as a package if the overall result of the settlement is just and reasonable. Under this approach, the Commission will not make a merits decision on whether each element of the settlement package is just and reasonable but will determine whether the overall package falls within a zone of reasonableness.[40] When the Commission takes this approach, it need not find that the settlement rate is exactly the rate the Commission would have found just and reasonable on the merits after litigation and need only find that the settlement rate falls within a zone of reasonableness. The Commission must also find under this approach that the contesting party would be in no worse position under the settlement than if the case were litigated.

34. The Commission employed this approach not only to honor the intent of the parties that the Settlement Agreement be considered as a package,[41] but also because the settlement contains several complex and interrelated features that make considering it as a package more appropriate than considering its individual parts.[42] The Commission went on to address each of the contested issues however, not to make a merits determination on each issue (which would be the first approach of *Trail-*

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[40] *See Trailblazer*, 85 FERC at 62,342; *order on reh'g*, 87 FERC at 61,440.

[41] *See Trailblazer, order on reh'g*, 87 FERC at 61,440 (when parties make clear that they want their settlement considered as a package, the Commission will try to honor parties' intent).

[42] June 16 Order at P 69.

blazer), but to validate our conclusion that the settlement package is just and reasonable.

35. Contrary to the arguments of IECG, the record contains substantial relevant evidence supporting the Commission's determination that the Settlement Agreement, and particularly the transition period, is just and reasonable. In particular, the record evidence in this proceeding, developed mostly during the year-long hearing on the LICAP demand curve mechanism, focuses on the cost of new entry (CONE), a key factor in determining appropriate rates for capacity.[43] This cost of new entry evidence[44] was central to the demand curves and resulting estimated prices presented at hearing and ultimately used to determine a reasonable range of prices in the June 16 Order.[45] This evidence of capacity costs is directly relevant to determining just and reasonable rates for capacity.

36. We disagree with the contentions of IECG that this evidence is irrelevant because it was developed in connection with the LICAP market design, which the Settlement Agreement abandoned in favor of FCM. ISO-NE is correct that while the market design used to determine the price may differ, both mechanisms provide a framework for purchasing the same product: capacity that is capable of producing energy when needed. As a

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[43] *See, e.g.*, Prepared Direct Testimony of John J. Reed, on behalf of ISO-NE, filed August 31, 2004 in Docket ER03-563-030.

[44] *See* Initial Decision at P 323-87.

[45] The price range used by the Commission covered a multi-year period, from 2007-2010, for different regions of New England. The lower and upper bounds of that range for 2007 were $1.91/kW-month and $7.63/kW-month respectively; lower and upper bounds of that range for 2010 were $2.53/kW-month and $16.16/kW-month.

result, the underlying evidence of the price of the capacity product is still relevant.

37. Maine Parties and Objecting Parties assert that the Commission cannot compare the transition rates under the Settlement Agreement to the rates that would result from the LICAP mechanism because the LICAP mechanism was adopted in an Initial Decision only and was not adjudicated by the Commission. In response, we note that Maine Parties (and others generally requesting rehearing of our application of *Trailblazer*, particularly to the transition period rates) appear to misstate the requirements of the second approach explained in *Trailblazer*. Under the second approach, the inquiry is whether the overall package of the settlement falls within "the broad ambit of various rates which may be just and reasonable."[46] This approach also requires that the Commission analyze whether those contesting the settlement would be in a worse position under the settlement than if the case were litigated; "this approach does not necessarily result in a binding merits determination on the individual issues in the proceeding, but it may involve some analysis of the specific issues raised by the settlement in order to determine whether the result under the settlement is not worse for the contesting party than the *likely result* of continued litigation."[47] It is the *likely* result of litigation that is used as a measuring stick, not an exact merits finding the Commission would have made if litigation had continued. Therefore, it was not necessary that the Commission conclude in the June 16 Order that it would have adopted any particular demand curve, as some of those requesting rehearing suggest. The range of possible outcomes discussed in the June 16 Or-

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[46] *Trailblazer*, 85 FERC at 62,343.

[47] *Trailblazer, order on reh'g*, 87 FERC at 61,440 (emphasis added).

der adequately supported our determination that the transition rates are just and reasonable.

38. Moreover, IECG is incorrect when it asserts that the Commission presented no methodology, analysis or formula to support its conclusion that the transition mechanism is a just and reasonable component of the settlement. Quite the opposite, the Commission discussed the rates under the transition mechanism at length in the June 16 Order. Consistent with the second approach of *Trailblazer*, the Commission compared the rates under the transition mechanism with a range of likely outcomes of continued litigation. The Commission did not establish that range in a vacuum, and instead considered a range of rates that might have resulted from continued litigation on the LICAP mechanism. That range of rates was derived directly from substantial record evidence in the hearing, and from it, the Commission reached a conclusion under the second approach of *Trailblazer*; it found that those objecting to the settlement would be in no worse position under the settlement than if the case were litigated. Not only is this analytical approach fully consistent with *Trailblazer*, it also meets the Federal Power Act (FPA) requirement that rates must be just and reasonable. As we stated in the June 16 Order, "[a] just and reasonable rate is not a product of any single formula, but is instead a rate within a broad ambit of various rates which may be just and reasonable."[48]

39. As discussed below, we also deny requests for rehearing specifically addressing the transition mechanism and the rates under that mechanism, and reiterate our

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[48] *See Belco Petroleum Corp. v. FERC*, 589 F.2d 680, 689 (D.C. Cir. 1979), *citing Permian Basin Area Rate Cases*, 390 U.S. 747, 767 (1968); *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 602 (1944); *FPC v. Natural Gas Pipeline Co.*, 315 U.S. 575, 585-86 (1942).

finding that, insofar as they are one component within a greater package of just and reasonable reforms, the transition payments serve as a reasonable bridge to the FCM.

40. First, in response to arguments (particularly from Objecting Parties) that the transition payment rates are not justified, we note our discussion above regarding the application of substantial record evidence to the transition payments. As discussed there, in the June 16 Order, the Commission compared the transition payments to a range of potential rates that could result under the LICAP mechanism to determine, consistent with *Trailblazer*, that those opposing the Settlement Agreement would be in no worse position under the Settlement Agreement than they would have been through continued litigation. The Commission used estimated prices developed from substantial record evidence on the CONE developed at the hearing in this proceeding, and found that the transition payments were well within the "broad ambit" of just and reasonable rates.[49] Accordingly, the Commission justified the transition payments as one component of the overall just and reasonable package represented by the Settlement Agreement.

41. In a related argument, Objecting Parties assert that, if the Commission had selected different proposed demand curves upon which to base price projections, a different result would have emerged. The Commission finds that relying on price projections using Maine and Vermont's and ISO-NE's proposed demand curves establishes a reasonable range of capacity prices for comparison. The projections that established the upper bound of the range were developed by James Daly, witness for a

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[49] *Id.*

coalition of parties, including the Attorney General of Massachusetts (AG Mass), NSTAR and The Energy Consortium, using the ISO-NE demand curve proposal.[50] Moreover, as we noted in the June 16 Order, Maine Parties relied upon those projections in their Initial and Reply briefs in the LICAP proceeding.[51] In establishing the lower range of price projections, the Commission selected price projections developed by ISO-NE, using the demand curve proposed by Maine and Vermont.[52] Record evidence contained an array of other demand curve proposals upon which to base price projections. Many of those from parties representing load would have shown prices lower than those produced using the Maine and Vermont curve and thus may have resulted in prices lower than the transition payments. Alternatively, those from suppliers would have shown prices much higher than the transition payments. If the Commission relied only upon demand curves proposed by parties representing load, the transition payments may have appeared excessive; relying only on demand curves proposed by suppliers would imply that the transition payments were inadequate. We conclude that relying on proposed demand curves from a single sector would have been unreasonable. As ISO-NE notes, the Commission may apply its expertise to the record before it and draw reasonable conclusions from that record in reaching a decision.

42. Objecting Parties note that the Commission previously rejected a transition mechanism proposed by ISO-NE. In the June 2 Order, the Commission deferred implementation of the initial LICAP proposal filed by

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[50] June 16 Order at P 94-99.

[51] *Id.* at P 97.

[52] Moreover, the Commission notes that these price projections were not adjusted to account for updated installed capacity requirement.

ISO-NE. That initial LICAP proposal included a series of transition mechanisms; Objecting Parties' comparison of these earlier transition mechanisms with the transition mechanism established in the Settlement Agreement is unavailing. First, the initial LICAP proposal failed to win requisite support in the stakeholder process, garnering 58 percent of the NEPOOL Participant Committee vote. In contrast, the Settlement Agreement has far larger and broader support: only eight of 115 parties to the settlement proceedings formally opposed the Settlement Agreement. Moreover, the NEPOOL Participants Committee voted, with 78.46 percent to support the Settlement Agreement, with support from all six voting sectors.[53] As we noted in the June 16 Order, while the level of support for the Settlement Agreement is not dispositive, the Commission can give weight to the broad-based support the Settlement Agreement received.[54] Moreover, we stated in the June 16 Order that the settlement "resolves all of the outstanding issues in a difficult, contentious and lengthy matter."[55]

43. Second, in contrast to the settlement, the initial LICAP proposal did not imply a final resolution to resource adequacy issues in New England. In filing the initial LICAP proposal, ISO-NE indicated that discussions

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[53] June 16 Order at P 15.

[54] *Id.* at P 73, *citing Laclede Gas Co. v. FERC*, 997 F.2d 936, 946 (D.C. Cir. 1993); *NorAm Gas Transmission Co. v. FERC*, 148 F.3d 1158, 1164-65 (D.C. Cir. 1998).

[55] June 16 Order at P 66; *see also Laclede Gas Co.*, 997 F.2d at 947 (while not dispositive, Commission may "weigh the prospects for protracted litigation" when deciding whether a settlement should be approved), *citing. c.f., Towns of Concord, Norwood and Wellesley v. FERC*, 997 F.2d 67, 76 (D.C. Cir. 1992) (indicating that the Commission may consider the time and expense of reconstructing past overcharges when constructing a remedy).

among regional stakeholders regarding a long-term resource adequacy mechanism were to continue and that "the filed proposal may be modified or replaced by a different long-term regional resource adequacy mechanism."[56] The Commission noted that the lengthy stakeholder proceedings in 2003 and 2004 failed to produce consensus and stated that it would be inappropriate to direct ISO-NE and stakeholders to continue working to develop a modified LICAP proposal.[57]

44. Third, in addition to transition payments, the initial LICAP proposal contained other design components that led the Commission to the conclusion that the proposal, as filed, would not resolve reliability compensation issues in New England. The initial LICAP proposal had a transition mechanism that involved not only fixed payments but also a series of price caps in import-constrained regions.[58] Moreover, the Commission also found that the specific regions proposed "did not adequately reflect where infrastructure investment is needed."[59] Finally, the Commission stated that ISO-NE had proposed a methodology that "may understate the level of capacity that may be transferred between ICAP regions."[60] In contrast to the initial LICAP proposal, the FCM uses a different methodology for stating capacity between capacity zones (or regions)[61] and provides a market de-

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[56] Compliance Filing of ISO-NE at 52, Docket No. ER03-563-030, filed March 1, 2004.

[57] June 2 Order at P 71.

[58] *Id.* at P 69.

[59] *Id.* at P 2.

[60] *Id.* at P 3.

[61] In the initial LICAP proposal, ISO-NE sought to measure transfer capacity across constrained ICAP regions using a methodology ("At Criteria") that may have underestimated actual amount of real

sign that appropriately determines capacity zones based on the identification of binding transmission limits.

45. We concluded in the June 16 Order (pursuant to *Trailblazer*) that the transition payments were a just and reasonable component of the package embodied by the Settlement Agreement. Objecting Parties offer no persuasive support for their assertion that the transition payments serve no regulatory purpose and are only "pure largesse" intended only to gain supplier sign-on. Moreover, resources that receive transition payments must, in exchange, meet all of the obligations of a capacity resource, which include the obligation to bid into the day-ahead and real-time markets and, whenever accepted in the markets, to forego the opportunity to sell into markets in other regions. As we note above, we concluded in the June 16 Order that the transition payments, while not ideal, are just and reasonable as a bridge to the full implementation of the FCM.

46. Moreover, Objecting Parties' argument that suppliers can receive transition payments without any limitation ignores the provisions of the Settlement Agreement, fully addressed in the June 16 Order, which adjust transition payments for availability during critical hours of need.[62] We address Objecting Parties' related arguments regarding the relationship between the transition payments and RMR agreements in the section that follows.

47. Finally, in response to Maine Parties' assertion that the lack of a locational element in the transition pay-

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time electric flow the transmission interface is capable of accommodating. However, ISO-NE, in subsequent testimony changed its position, recommending the use of a methodology ("As-Is"), meaning that system would be modeled using all available capacity.

[62] June 16 Order at P 103.

ments makes them irreconcilable with the Commission's prior determinations in this case, we emphasize that the transition mechanism is just that; a temporary mechanism to serve as a bridge until the FCM is fully implemented in 2010. In the June 16 Order, we concluded that the FCM itself appropriately recognizes location.[63] The lack of a location element in this temporary transition period does not invalidate our conclusion that the Settlement Agreement as a package, including the transition mechanism and the FCM, is just and reasonable.

2. Continuation of RMR Agreements

48. The currently applicable RMR agreements in New England are scheduled to terminate upon the implementation or effectiveness of a locational ICAP mechanism. The Settlement Agreement explicitly states that the beginning of the first commitment period (June 1, 2010) will be considered to be the implementation or effectiveness of a locational ICAP mechanism for purposes of these RMR agreements. The Settlement Agreement states that nothing prejudices the rights of any party to challenge, seek to terminate or support an RMR agreement on any other grounds or restrict any party's rights to seek, agree to or oppose any RMR modifications.

49. In the June 16 Order, the Commission approved the proposed timeline for the termination of RMR agreements. The Commission found that the June 2010 termination date of RMR agreements is consistent with the express terms of the RMR agreements and the Commission's intent that those contracts terminate when a capacity market mechanism is fully implemented. The Commission noted that the transition payments will be netted against RMR revenues, protecting against over-recovery.

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[63] *Id.* at P 122.

The Commission further noted that the Settlement Agreement explicitly states that participants do not waive rights to challenge the need for RMR contracts, based on, *e.g.*, changes in a generator's compensation or changes to system infrastructure. [64]

Requests for Rehearing

50. Objecting Parties assert that the Commission should not allow RMR agreements to remain in place until 2010, during the period when suppliers are receiving transition payments, and should impose a moratorium on the filing of new RMR agreements. Objecting Parties argue that the Commission appears willing to overlook the disruptive effect RMRs have on the wholesale markets while not acting to curb the filing of new RMR agreements. In approving the Settlement Agreement, Objecting Parties state that the Commission is allowing generators to choose between the higher of market or cost-based rates, a defect that the Commission sought to remedy when it ordered implementation of a market-based mechanism in this proceeding. Objecting Parties argue that generators should not be allowed to receive transition payments on top of cost-of-service rates, which Objecting Parties argue were granted without considering additional revenues from the locational forward reserves market and from transition payments. Objecting Parties argue that to the extent that the Commission allows the transition payment provisions to remain in the Settlement Agreement, it should modify the Settlement Agreement to provide that all existing RMR agreements will terminate upon the initiation of transition payments.

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[64] *See* Settlement Agreement at section XIII.F.

Answers

51. ISO-NE states that, insofar as RMR agreements terminate when a true market commences, the Commission's decision to approve the Settlement Agreement is consistent with the goals of reducing the need for RMR agreements and replacing them with a market-based mechanism. ISO-NE also argues that the Settlement Agreement contains express language, cited in the June 16 Order,[65] that participants do not waive their rights to challenge the need for RMR contracts, given changes in a generator's compensation or changes to system infrastructure.

Commission Conclusion

52. The Commission notes that Objecting Parties requested identical relief in their comments in opposition to the Settlement Agreement.[66] The Commission will not grant rehearing on this issue. As we stated in the June 16 Order, the Commission has consistently accepted RMR agreements for a term that expires upon implementation of a locational mechanism, which the Settlement Agreement expressly provides as the beginning of the first FCA commitment period.[67] We reiterate here our finding that the FCM represents an appropriate locational capacity mechanism upon which to base the termination of existing RMR agreements. Until that time, existing RMR agreements will remain in effect.

53. The Commission again rejects arguments that generators will be able to receive both cost of service rates

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[65] June 16 Order at P 166.

[66] See Comments in Opposition to Settlement Agreement of Objecting Parties at 25 (filed March 27, 2006).

[67] *See* section VIII.F of Settlement Agreement.

and transition payments. As the Settlement Agreement makes clear,[68] transition payments will be netted against RMR revenues, and thus there will be no opportunity for a generator to receive transition payments on top of the full cost of service rates under the RMR agreement. Thus any payment to an RMR generator that exceeds the transition payment level will only represent that generator's Commission-approved cost-of-service rate under the RMR agreement. Also, we again note that the Settlement Agreement explicitly states that participants do not waive their rights to challenge the need for RMR contracts, based on, *e.g.*, changes in a generator's compensation or changes to system infrastructure.[69] Finally, Objecting Parties' assertion that the Commission did not consider the impact of the locational forward reserves market is incorrect; the Commission fully addresses this issue in the June 16 Order.[70]

3. Determination of Separate Capacity Zones

54. Under the Settlement Agreement, before each auction, ISO-NE will determine capacity zones based on an identification of transmission limits that may bind. In instances where transmission limits are expected to bind (accounting for predicted upgrades that will be on-line by the commitment period), ISO-NE will designate separate capacity zones and hold separate but simultaneous auctions.

55. In the June 16 Order, the Commission accepted the locational feature of the FCM as contributing to the overall justness and reasonableness of the Settlement Agreement as a package and satisfying the directive in

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[68] *See* Settlement Agreement at section VIII.E.

[69] *See* Settlement Agreement at section XIII.F.

[70] June 16 Order at P 131.

prior Commission orders that the capacity market take into account location. The Commission stated that transmission constraints may restrict the ability to deliver energy from some locations to others, and a market design for capacity should reflect transmission constraints to send correct price signals for investment. The Commission stated that it believed that the settlement provides for a way to recognize transmission constraints that is, on balance, reasonable.[71]

Requests for Rehearing

56. In comments opposing the Settlement Agreement, Maine Parties argue that the determination of whether binding constraints exist (which will then result in separate import constrained zones) is inferior to allowing actual price separation to occur as part of the auction process. The Commission rejected the Maine Parties' approach, stating that adopting the Maine Parties' proposal may provide sellers of capacity the incentive to withhold capacity to create price separation and separate capacity zones where they are not necessary. In such cases, the Commission concluded that such constraints would bind because of the exercise of market power, and not because of actual physical limitations arising from competitive market conditions.[72]

57. In their rehearing request, Maine Parties state that the Commission's market power rationale is flawed because it advocates the elimination of opportunities for market power abuse by simply eliminating the market (auction) approach. Maine Parties argue that by the Commission's logic, the fact that it might be easier to exercise market power in a locational energy market than

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[71] *Id.* at P 122.

[72] *Id.* at P 122-124.

in a non-locational market suggests that the locational energy market should be eliminated too. Maine Parties assert that the Commission's conclusion fails to explain the distinction between the potential problems of market abuse in the capacity market versus those in the energy market, where price separation is allowed to occur through a market approach (with vigilance and safeguards against the exercise of market power). Maine Parties assert that the settlement contains a number of features specifically designed to reduce or eliminate market power, and these may well be adequate to reduce, if not eliminate, the impact of market power abuse in constrained areas.

Answers

58. ISO-NE asserts that the process for designating capacity zones in the Settlement Agreement is an alternative locational feature that should yield similar results to the process advocated by Maine Parties. ISO-NE contends that the approach in the Settlement Agreement has the added advantage of reducing the risk of the exercise of market power.

Commission Conclusion

59. We will deny the rehearing request of the Maine Parties on this issue. We have accepted pre-established zones in capacity markets elsewhere, such as New York,[73] and we will not modify the settlement provision that would determine capacity zones in advance of the auction. We disagree with Maine Parties' assertion that the order advocates elimination of the market, or the elimination of the locational feature of the market, in an effort to elimi-

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[73] *See New York Independent System Operator, Inc.*, 90 FERC ¶ 61,319 (2000), and *New York Independent System Operator, Inc.*, 93 FERC ¶ 61,186 (2000).

nate market power. To the contrary, the June 16 Order accepts the use of a forward capacity market and, as part of that, determining capacity zones before holding auctions based on transmission constraints created by competitive market conditions.

60. We are not persuaded at this time that it is necessary to establish capacity zones in areas where such zonal boundaries do not appear, in advance of the auction, to be justified. As we noted in the June 16 Order, if auction results were allowed to establish local capacity zones, sellers of capacity may have an incentive to withhold capacity (thereby creating separate capacity zones where they are not necessary) to increase the capacity price in the import zone. By establishing zones in advance as provided in the settlement, the financial advantage from withholding would be reduced or eliminated because the price on the import side of the zone could not rise above the price elsewhere in the zone.

61. We acknowledged in the June 16 Order that there may be advantages to the approach advocated by the Maine Parties. It is possible that additional transmission congestion not foreseen by ISO-NE may develop as a result of competitive conditions during the FCA within the pre-established zones.[74] However, the settlement pro-

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[74] The Maine Parties incorrectly summarized the June 16 Order as stating that price separation in an auction mechanism would always be the result of the exercise of market power. The Maine Parties apparently base their conclusion on the sentence in Paragraph 123 of the order that reads: "These constraints would bind only because of the exercise of market power. . . ." However, the phrase "these constraints" refers to the constraints that would arise from the situation described in the previous sentence, where "sellers of capacity would have the incentive to withhold capacity to create price separation and separate capacity zones where they are not necessary." That is, "these constraints" refers to constraints that arise when

vides a mechanism to monitor for this possibility. Specifically, the settlement requires ISO-NE's Market Monitor to analyze the operations and effectiveness of the FCM no later than 180 days after the second FCA is conducted, as well as annually in its annual markets report. The reports will help evaluate whether the capacity zones established by ISO-NE in advance of the auctions turn out to contain significant transmission congestion within them. If the reports conclude that significant intrazonal congestion occurs, parties may file to change this feature of the settlement.

4. Issues Regarding Export Constraints to/ from Maine

62. Maine Parties filed affidavits (prepared by Dr. Thomas Austin) with their comments on the Settlement Agreement, which, Maine Parties argue, offered evidence of various flaws in the settlement. Maine Parties assert that the evidence presented in Dr. Austin's testimony demonstrated that the Settlement Agreement cannot be found to be just and reasonable. Dr. Austin argued that: 1) data from energy markets congestion and ISO-NE's Regional System Plan show that Maine is export constrained; 2) there are plans for new generation to be developed in Maine; 3) generators like FPL Energy have experienced increased earnings so additional revenues from capacity payments are not needed to keep hydro and nuclear plants operational; 4) the transition payments do not contain a PER offset,[75] and the assumed

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sellers withhold capacity. Thus, a correct summary of Paragraph 123 would be that constraints that arise when sellers withhold capacity would bind only because of the exercise of market power.

[75] The PER offset was designed to adjust the LICAP payments with the energy market profits from a benchmark unit to assure that the LICAP Payments did not double-count energy rents.

PER in ISO-NE witness LaPlante's analysis is too low. In their request for rehearing, Maine Parties argue that the June 16 Order failed to address these arguments, thus rendering the Commission's decision arbitrary and capricious.

63. Contrary to Maine Parties' assertion, Dr. Austin provided data which showed that the congestion component of the Maine's LMP was negative 25.8 percent of the time in 2005 and during 42.9 percent of all real time hours in July 2005. Maine Parties further assert that the ISO-NE Regional System Plan shows that Maine is export constrained:

> The output of Maine generators is sometimes constrained by export limitations to the south and west. When constrained, the Orrington–South, Surowiec–South, Maine–New Hampshire, Northern New England–Scobie + 394 line, Seabrook–South, and North–South transmission interfaces are indicative of Maine export limitations. One or more of these interfaces was constrained about 10.5% of the real-time hours during 2005.[76]

64. Maine Parties assert that there has been no rebuttal of Dr. Austin's testimony that additional wind and other generation projects planned for Maine would further exacerbate Maine's export-constraint. Maine Parties state that there is currently 1,000 MW of new non-gas-fired generation capacity "under construction, in the permitting process or under serious consideration by developers,"[77] and that such projects have expected in-service dates between 2006 and 2009.

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[76] Request for Rehearing of Maine Parties at 16.

[77] *Id.* at 17.

65. Maine Parties assert that, in not examining the costs and earnings of generators in Maine or valuing their products by location, the FCM Order cannot accomplish one of the Commission's stated goals in the proceeding—to ensure that existing generators are appropriately compensated. Maine Parties further assert that the FCM Order failed to address arguments that the windfall for existing power supplies will be exacerbated by the lack of a PER offset during the transition period. Maine Parties assert that without such an offset there will neither be a hedge against energy spikes nor any disincentive so as to prevent suppliers from raising energy prices during the transition period.

66. Maine Parties assert that genuine issues of material fact exist that cannot be resolved on the current record. Maine Parties argue that additional evidence is needed to determine the extent of the Maine export constraint, and how it would impact the auction and the prices paid by Maine. Given that assertion, Maine Parties request the opportunity to probe the underlying basis for ISO-NE's assertions regarding the frequency of the binding constraint between Maine and the Rest of Pool. Maine Parties suggest that options include: (1) conditional acceptance of the settlement; (2) severance of the contested issues and initiation of further procedures to resolve those issues; and (3) rejection of the entire settlement and initiation of a hearing.

67. On September 8, 2006, Maine Parties filed a motion to lodge additional evidence, asking the Commission to consider specific sections of the recently-issued National Electric Transmission Congestion Study conducted by the Department of Energy. Maine Parties argue that this evidence is directly relevant to its argument on rehearing (discussed below) that the transition payments

included in the Settlement Agreement should be lower for Maine since it is "generation-rich."

Answers

68. ISO-NE argues that Maine is not meaningfully export-constrained. First, ISO-NE argues that the LMP congestion component has no bearing on whether Maine is export-constrained. ISO-NE argues that a negative congestion component for Maine's LMP merely indicated that there was a binding transmission constraint somewhere in New England. ISO-NE also analyzed the degree to which the Maine-New Hampshire interface constraint was binding in 2005 and found it was binding during 74 real time energy market hours in 2005 (less than one percent of the time).

69. Finally, ISO-NE argues that there is a distinct difference between plans for new generation and actual installed generation. ISO-NE asserts that there is no record evidence: 1) to indicate that sufficient generation will come on-line during the transition period to make the Maine Parties' assertion of a binding export constraint reality; and 2) to identify specific projects and specific schedules.

70. ISO-NE asserts that the Maine Parties' pleading has no analysis of why some generators' profits should be considered to be greater than normal, what the source of those profits was, and what revenues are needed to keep various plants operational. ISO-NE further asserts that the hearing record demonstrates that many generators are earning insufficient revenues to continue operating or to support new investment. ISO-NE concludes by stating that generating companies will not be prompted to build new generation or to maintain unprofitable units on the basis of whether, in the aggregate, their generation portfolios are profitable.

Commission Conclusion

71. The Commission denies Maine Parties' request to modify the transition payments or to establish separate hearing procedures to address Maine Parties' contention that the state is export-constrained. Maine Parties' fundamental argument appears to be that Maine is export-constrained and, as such, should not be required to pay the full transition payment. Maine Parties have offered different options for resolving the issue: 1) modify Maine's transition payment to 2.00/kW-month for all years,[78] 2) reject the Settlement in its entirety, with "the matter set for hearing,"[79] or 3) reject the Settlement Agreement as proposed and "initiate proceedings to gather the substantial evidence necessary to reach a reasoned decision."[80]

72. The Commission did consider arguments presented in Dr. Austin's affidavits in approving the Settlement Agreement. Maine Parties' witness Austin provided several arguments in filed affidavits, many of which were devoted to establishing Maine as an export-constrained zone. However, the issue of Maine being export-constrained is not the subject of this proceeding. The Commission's responsibility in approving the Settlement Agreement was not to determine whether or not Maine is export-constrained. Rather, the Commission's responsibility is to ensure that rates are just and reasonable.

73. The Commission found that the transition payments agreed to by parties to the Settlement Agreement,

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[78] Comments in Opposition to Settlement Agreement of Maine Parties at 2 (filed March 27, 2006).

[79] *Id.* at 3.

[80] Request for Rehearing of Maine Parties at 2.

though "not ideal as a single market design element,"[81] represented one element of a just and reasonable package of reforms that was embodied in the Settlement Agreement. Relying on the second approach of *Trailblazer*, we determined that contesting parties would be in no worse position under the settlement than if the case were litigated.

74. The Commission will not initiate procedures to gather evidence and determine "appropriate capacity rates"[82] for the interim period, for Maine or any other states affected by the Settlement Agreement. The Commission reiterates that the transition rates are an essential element of a package that will establish a capacity procurement mechanism that resembles, quite closely, an alternative to the LICAP proposal presented by Maine Parties at Oral Argument. Second, Maine Parties' request here is an attempt to sever an issue from the proceeding. As the Commission stated in the June 16 Order, severance is inappropriate as the Settlement Agreement provides a capacity market construct (including a transition period) that will apply throughout New England.[83]

75. Maine Parties assert that absent an offset for PER during the transition period, the windfall for existing power supplies will be exacerbated. The Commission disagrees. We found that the transition payments fell within a reasonable range of prices. In that range we included projections from ISO-NE witness David LaPlante that included a PER figure of $0.48/kW-month[84]: those

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[81] June 16 Order at P 89.

[82] Request for Rehearing of Maine Parties at 23.

[83] June 16 Order at P 106.

[84] *See* Attachment 6 to the Settlement Agreement, filed March 6, 2006.

projections, less the PER offset, were still higher than the transition payments.[85] The Commission finds this to be a reasonable estimate of PER, given that the "PER offset is driven by the times when prices exceed the price of the 22,000 heat rate unit."[86] Moreover, as we discussed in the June 16 Order, the transition payments will be adjusted to account for unit performance during periods of high demand.[87]

76. We deny Maine Parties motion to lodge. It would be inappropriate to accept evidence at this extremely late date in this proceeding (after a dispositive order has been issued), since it would effectively deny parties the opportunity to respond to the evidence. In any event, the new evidence relates to whether Maine is export constrained, which is not the subject of this proceeding.

5. Acceptance of Section 4C of the Settlement Agreement

77. Section 4.C of the Settlement Agreement provides:

> From the Effective Date, absent the agreement of all Settling Parties to the proposed change, the standard of review for: (i) challenges to the Capacity Clearing Prices derived through the FCA and prices resulting from reconfiguration auctions provided for in the Settlement Agreement and in the Market Rules addressing the terms of the Settlement Agreement that are approved or accepted by the FERC pursuant to section 3, and (ii) proposed changes to section 11, Part VIII below (Agreements Regarding Transition Period) and the Market

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[85] *See id.* at 5, note 6 (ISO-NE witness LaPlante setting forth projected LICAP clearing prices less PER offset).

[86] Answer of ISO-NE at 19.

[87] June 16 Order at P 103.

> Rules implementing that part, shall be the "public interest" standard of review set forth in *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332 (1956) and *Federal Power Commission v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956) (the "Mobile-Sierra" doctrine), whether the change is proposed by a Settling Party, a non-Settling Party, or the FERC acting *sua sponte*. This Settlement Agreement does not impose the Mobile-Sierra standard on any provision of this Settlement Agreement or the Market Rules that address the terms of the Settlement Agreement except as expressly provided in this section 4.C.

78. In the June 16 Order, the Commission rejected calls from opponents of the Settlement Agreement to reject or modify this provision. First, the Commission noted that under section 4.C, the *Mobile-Sierra* "public interest" standard applies only to (1) the final clearing prices in the FCA and any reconfiguration auctions permitted under the Market Rules, and (2) the transition mechanism.[88] Thus, the Commission concluded that concerns expressed by IECG that this provision would broadly eliminate the ability of non-parties and the Commission to exercise their rights under the FPA were misplaced.[89] Next, the Commission found that section 4.C is fully consistent with current Commission policy permitting the use of similar provisions (including in contested settlements), and that there is no Commission or court precedent allowing a non-signatory to unilaterally seek changes to a *Mobile-Sierra* "public interest" contract under the "just and reasonable" standard.[90] Further, the Commission

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[88] June 16 Order at P 182.

[89] *Id.*

[90] *Id.* at P 183.

found that the *Mobile-Sierra* provision is reasonable because of several additional protections available to non-parties. Specifically, the Commission noted that it retains significant authority to protect non-parties, given that "the most attractive case for affording additional protection . . . is where the protection is intended to safeguard the interests of third parties."[91] Moreover, the Commission recounted the procedural safeguards built into the Settlement Agreement; in particular, the Commission noted that ISO-NE is required under the agreement to make an informational filing before each FCA and a section 205 filing after each FCA containing the results, both of which are considered under the "just and reasonable" standard.[92] Finally, the Commission concluded that section 4.C "appropriately balances the need for rate stability and the interests of the diverse entities who will be subject to the FCM."[93]

Requests for Rehearing

79. IECG and Maine Parties seek rehearing of the Commission's refusal to modify or eliminate section 4.C of the Settlement Agreement. IECG first contends that the Commission reads this provision too narrowly, and that it will apply to the market rules filed to implement the transition mechanism, contrary to the Commission's statements in the June 16 Order.

80. Further, IECG argues that the generally-applicable market rules and rates identified in the Settlement Agreement as subject to the "public interest" standard are not contracts eligible for *Mobile-Sierra* protection.

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[91] *Id.* at P 184, *citing Northeast Utilities Serv. Co. v. FERC*, 993 F.2d 937, 961 (1st Cir. 1993) (*Northeast Utilities I*).

[92] *Id.* at P 185.

[93] *Id.* P 186.

According to IECG, the principle underlying *Mobile-Sierra* is "that the parties to a contract should be held to the contract's terms," and thus the doctrine should not be used to prevent non-parties to a Settlement Agreement from challenging market rules or tariff rates that apply to everyone in a market, and consequently are not in and of themselves contracts.[94]

81. IECG also asserts that section 4.C represents an unlawful amendment to the NEPOOL governance structure. IECG states that under section 11.1.5 of the NEPOOL Participants Agreement, Governance Participants have the right to propose changes to the market rules and to have those proposed changes reviewed by the Commission under section 205 of the FPA, if there is support from a majority of the Governance Participants. IECG argues that section 4.C eliminates this right of Governance Participants without the necessary amendments to the Participants Agreement.[95]

82. IECG and Maine Parties argue that section 4.C unlawfully extinguishes their right under section 206 of the FPA to challenge rates as unjust and unreasonable, which the Settling Parties cannot do with their assent. IECG contends that such rights are statutory, and only Congress can abrogate those rights, not Settling Parties or the Commission.[96] Similarly, Maine Parties argue that while parties to a contract can voluntarily give up their

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[94] Request for Rehearing of IECG at 15.

[95] IECG states that Settling Parties did not follow the required procedures to amend the Participants Agreement, and that the Commission itself may not amend that agreement in the absence of substantial evidence in the record. *See id.* at 17-18.

[96] *Id.* at 18, *citing Atlantic City Electric Co. v. FERC*, 295 F.3d 1, 9-11 (D.C. Cir. 2002).

rights under the FPA, the Commission cannot deprive a party of those rights.

83. IEGC also notes that it is not a party to the Settlement Agreement, and thus is not bound by its terms. Instead of seeking a unilateral change to the Settlement Agreement, as the Commission states in the June 16 Order, IECG explains that it only "seeks to disentangle itself from a contract" that would improperly amend the NEPOOL Participants Agreement and interfere with its rights under that agreement and section 206 of the FPA. IECG asserts that contrary to the Commission's conclusion, there is ample precedent supporting its position that a settlement agreement may not bind the Commission or third parties to the "public interest" standard.[97] While recognizing that the Commission has recently changed course, IECG contends that this more recent course is inconsistent with the "contract law foundations of *Mobile-Sierra*," including "the principle that a contract binds those who sign it and does not bind those who do not."[98] IECG urges the Commission to return to its earlier precedent.

84. Finally, IECG and Maine Parties both disagree with the Commission's conclusion that section 4.C does not operate to the detriment of non-settling parties, arguing that while the Commission may still retain authority to protect its interest, the "public interest" is still a more

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[97] Request for Rehearing of IECG at 19-20, *citing Westar Generating, Inc.*, 100 FERC ¶ 61,255 at 61,917 (2002); *PJM Interconnection, LLC*, 96 FERC ¶ 61,206 at 61,878 (2001); *Cities of Anaheim and Riverside, California*, 90 FERC ¶ 61,236 at 61,754 (2000); *Montana Power Co.*, 88 FERC ¶ 61,019 at 61,051 (1999); *Carolina Power & Light Co.*, 67 FERC ¶ 61,074 at 61,205 (1994).

[98] *Id.* at 21.

difficult standard to meet. Maine Parties note that no matter how limited the impact of the provision may be, the Commission may still not diminish the rights of non-signatories under the FPA. Moreover, IECG argues that the Commission acted irresponsibly by approving this *Mobile-Sierra* provision, given that it has no time limits and thus will bind the Commission in perpetuity to certain elements of an untested market design. Maine Parties state that Commission precedent indicates that it is appropriate to reject the application of the "public interest" standard where necessary to preserve the ability to protect broad market interests, and that preserving the ability to challenge all aspects of the capacity market is critical here because the market design is new and untested.

Answers

85. ISO-NE responds that current Commission policy allows application of the "public interest" standard to both the Commission and non-parties to a settlement. Additionally, it objects to IECG's argument that market rules and tariff rates of general applicability are not contracts to which *Mobile-Sierra* can be applied, stating that the Settlement Agreement is a contract governing the process for determining rates and market rules, and that the Commission has applied the *Mobile-Sierra* doctrine to contracts setting rates. NEPOOL also asserts that contrary to IECG's argument, established law and precedent hold that a tariff is a contract.[99] ISO-NE also notes that the Commission still "retains its indefeasible statutory right" to examine and require changes to the

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[99] Answer of NEPOOL at 3-4, *citing in part New York State Electric and Gas Corp. v. New York Independent System Operator, Inc.*, 168 F.Supp. 2d 23, 27 (N.D.N.Y 2001) (holding that New York ISO tariffs are contracts).

rates and market rules if required by the public interest.[100]

86. Moreover, ISO-NE and NEPOOL both argue that application of the "public interest" standard as set forth in section 4.C is appropriate, given: (i) that it applies narrowly to the final capacity clearing prices and transition mechanism once approved, (ii) that the Settlement Agreement includes certain procedures to review the FCA results under section 205 before they become final and to file the transition market rules under section 205, and (iii) because price certainty is critical in this instance to ensure that risks to investors and costs to consumers are kept low.

87. NEPOOL responds to IECG's argument that section 4.C has amended or limited the rights of participants under the NEPOOL Participants Agreement. First, NEPOOL notes that the Participants Agreement is among ISO-NE, NEPOOL and Governance Participants that have signed the agreement but have not joined NEPOOL, and that section 17.2 of that agreement expressly provides that it does not grant any separate rights or benefits to non-signatories such as IECG. Moreover, NEPOOL argues that section 11.1.5 of the Participants Agreement does not limit NEPOOL or any individual participant from entering into a settlement, and NEPOOL itself voted to approve the Settlement Agreement. Further, it contends that the Settlement Agreement does not provide for the adoption of market rules and procedures outside of the stakeholder process, as IECG contends, but instead provides that such rules

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[100] Answer of ISO-NE at 30, *citing Midwest Independent Transmission System Operator, Inc.* 115 FERC ¶ 61,174 at P 40 (2006) (*citing Metropolitan Edison Co. v. FERC*, 595 F.2d 851, 856 n.29 (D.C. Cir. 1979)).

will be developed within the stakeholder process, and that IECG and all other participants may consider and vote on those rules within that process. With regard to the filing of market rules governing the transition period, both NEPOOL and ISO-NE note that the Settlement Agreement provides that those rules will be filed under the just and reasonable standard of section 205 of the FPA.

Commission Conclusion

88. The Commission denies these requests for rehearing. IECG and Maine Parties have presented no new arguments that were not addressed in the June 16 Order, and have not persuaded us to revisit our conclusions in that order.

89. First, we disagree with IECG that the Commission read section 4.C of the Settlement Agreement too narrowly in the June 16 Order. Under that provision, the market rules developed and filed with the Commission under the Settlement Agreement will be reviewed under section 205 of the FPA. In an order issued contemporaneously with this order, the Commission rules on the market rules implementing the transition period under the "just and reasonable" standard of section 205.[101] While under the terms of section 4.C the "public interest" standard will attach to those market rules after they are finalized in that proceeding, we conclude that this limited application of *Mobile-Sierra* is reasonable, especially since those market rules will only be in place temporarily until the FCM begins.

90. We also reject IECG's contention that market rules and tariffs are not contracts to which *Mobile-Sierra* can apply. As NEPOOL points out, tariffs have been held to

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[101] [cite to companion order]

be analogous to contracts. Additionally, the Commission has on many occasions accepted the application of the "public interest" standard to settlement agreements and contracts setting forth rates.[102] Moreover, the *Mobile-Sierra* provision in this case applies to the Settlement Agreement and the rates resulting from that agreement. As noted above, the market rules implementing the settlement will be made under section 205 and considered by the Commission under the "just and reasonable" standard. As a result, the Settlement Agreement does not prevent non-parties from challenging the market rules that will implement the settlement.

91. Further, we reject IECG's assertion that section 4.C represents an improper amendment to the NEPOOL Participants Agreement. As NEPOOL points out, nothing in the sections of that agreement cited by IECG prevent NEPOOL from entering into a settlement. NEPOOL, as a body, approved the Settlement Agreement by stakeholder vote, as provided for in its governing documents. Additionally, the Settlement Agreement provides that further filings made to implement it (including market rules) will be developed in the stakeholder process and filed under section 205 of the FPA. It does not in any way amend the stakeholder procedures provided for in the Participants Agreement as IECG asserts.

92. The Commission previously rejected arguments that section 4.C unlawfully limits the rights of non-parties to the Settlement Agreement under the FPA, and that the Commission and non-parties to a Settlement Agreement cannot be bound to the "public interest" standard. In the June 16 Order, we noted that the Commission has rou-

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[102] *See, e.g., infra* note 104.

tinely permitted the use of similar provisions in settlement agreements, including contested settlements.[103] Moreover, we noted that the Commission has stated on several recent occasions, "there is no Commission or court precedent that supports a finding that a non-signatory may unilaterally seek changes to a *Mobile-Sierra* 'public interest' contract under the 'just and reasonable' standard of review."[104] While IECG cites to earlier Commission cases supporting its position that a settlement agreement may not bind the Commission or third parties to the "public interest" standard, the Commission has more recently consistently accepted application of that standard to the Commission or third parties to a settlement agreement.[105] IECG and Maine Parties have raised no new arguments that persuade us to revisit our conclusions there.

93. Non-signatories to the Settlement Agreement are protected here, and as a result, we reject the notion that we have acted "irresponsibly" by accepting section 4.C. In the June 16 Order, we explained that the Settlement

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[103] *See, e.g., Midwest Independent System Operator, Inc.*, 115 FERC ¶ 61,174 (2006); *Midwest Independent System Operator, Inc.*, 110 FERC ¶ 61,177 (2005); *Midwest Independent System Operator, Inc.*, 110 FERC ¶ 61,380 (2005); *Pennsylvania-New Jersey-Maryland Interconnection*, 105 FERC 61,294 (2003), *reh'g denied*, 108 FERC ¶ 61,032 (2004); *Vermont Electric Cooperative, Inc.*, 114 F.E.R.C. ¶ 61,220 (2006); *Calpine Construction Finance Company, L.P.*, 114 F.E.R.C. ¶ 61,217 (2006); *Hermiston Power Partnership*, 114 F.E.R.C. ¶ 61,204 (2006); *Central Maine Power Company*, 114 F.E.R.C. ¶ 61,184 (2006); *San Diego Gas & Electric Company*, 114 F.E.R.C. ¶ 61,158 (2006); *Wisconsin Power & Light Co.*, 106 FERC ¶ 61,112 (2004).

[104] *Pennsylvania-New Jersey-Maryland Interconnection*, 108 FERC ¶ 61,032 at P 7, *citing Public Utilities Commission of the State of California*, 105 FERC ¶ 61,182 at P 50 (2003).

[105] See *supra* notes 103-104.

Agreement provides for thorough review of the final auction clearing prices by the Commission and any interested parties.[106] In particular, the Settlement Agreement provides that ISO-NE will make both an informational filing prior to the auction that includes information regarding the zones to be used and qualifying bids, and a section 205 filing following the auction containing the results. Because the limited *Mobile-Sierra* provision in section 4.C does not apply to these filings, parties may challenge them under the "just and reasonable standard" and the Commission will address such challenges under that standard. These provisions also address concerns that the FCM market design is untested; these regular filings will reveal any unanticipated problems with that design, giving the parties an opportunity to address them under the just and reasonable standard.

94. Additionally, as we explained in the June 16 Order, even under the "public interest standard," the Commission retains significant authority to protect non-parties to the Settlement Agreement and the public;[107] as ISO-NE correctly states, we retain an "indefeasible right" under the FPA to examine the FCM and require changes if required by the public interest.[108]

95. Finally, as ISO-NE and NEPOOL point out in their answers, price certainty is important to ensure that the FCM achieves its goals of attracting and retaining generators needed for reliability. As we stated in the June 16 Order, stability is of particular importance in this

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[106] June 16 Order at P 185.

[107] *Id.* at P 184.

[108] *See Maine Public Utilities Commission v. FERC*, 454 F.3d 278, 283 (D.C. Cir. 2006), *citing Papago Tribal Utility Authority v. FERC*, 723 F.2d 950, 953 (D.C. Cir. 1983).

case, given that these proceedings were initiated in part because of the unstable nature of ICAP revenues and the negative effect that it has had on New England's infrastructure.[109] Section 4.C achieves this stability while still allowing the Commission and the parties to thoroughly and regularly review and raise objections to the prices produced by the FCM.

6. **Other Issues**

(i) **Finding that the Existing ICAP Market is Unjust and Unreasonable**

96. In the June 16 Order, the Commission noted that it had previously declared that the existing ICAP market is unjust and unreasonable under section 206 of the FPA.[110] The Commission stated that as explained in the June 2 Order, the April 25 Order directed revisions to the ISO-NE tariff "pursuant to section 206 of the [FPA]" to "implement . . . location or deliverability requirements in the ICAP or resource adequacy market . . . so that capacity within [designated congestion areas] may be appropriately compensated for reliability."[111] In the July 24 Order, the Commission further clarified that it was acting under section 206 of the FPA and formally stated that it "found that Market Rule 1 created an unjust and unreasonable result" because RMR agreements, and the need for such agreements, caused an extensive disruption

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[109] June 16 Order at P 186, *citing in part Potomac Electric Power Co. v. FERC*, 210 F.3d 403, 409 (D.C. Cir. 2000) ("The court has repeatedly emphasized the importance of contractual stability in a number of cases involving the *Mobile-Sierra* doctrine").

[110] *Id.* at P 203.

[111] *Id., citing* June 2 Order at P 29 and April 25 Order at P 33, 37.

to wholesale markets.[112] The Commission also concluded that the record contains substantial evidence regarding the inability of generators to earn sufficient revenues in the current market, both to continue operating or to support new investment. The Commission further noted that the increase in RMR agreements in New England provided further substantial evidence that generators are failing to recover their costs under the existing market design.

Requests for Rehearing

97. Objecting Parties state that in the FCM Order, the Commission asserts that it has found the existing ICAP market to be unjust and unreasonable. Objecting Parties argue that there is no basis for that finding. Objecting Parties assert the Commission's finding was limited to a discrete set of resources, *i.e.*, seldom-run units needed for locational reliability, not the entire ICAP market. Thus, Objecting Parties contend that at no time in the proceeding has there been any demonstration or finding by the Commission that all generation resources within NEPOOL need additional revenue through a revised capacity market. Objecting Parties argue that, in fact, record evidence is unequivocal: classes of generation, such as coal and nuclear are earning more than sufficient returns. Objecting Parties state that claims that the existing market is not working cannot be verified when there is an undisputed surplus of installed capacity in New England. Objecting Parties assert that the pricing in the current ICAP market reflects oversupply conditions and that should such conditions change, prices will adjust appropriately.

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[112] *Id.* at P 203, *citing* June 2 Order at P 29 and July 24 Order at P 33.

Answers

98. ISO-NE asserts that the Commission determined the existing ICAP market to be unjust and unreasonable several years ago and that "the time has long since passed" to seek rehearing. ISO-NE argues that Objecting Parties are barred procedurally from seeking rehearing of the Commission's determination that the existing ICAP market is unjust and unreasonable. ISO-NE states that Objecting Parties do not claim that the Commission's finding was made in the June 16 Order, and that Objecting Parties acknowledge that the Commission made this finding in previous orders. ISO-NE argues that there also is ample record evidence supporting this determination, including, ISO-NE states, "almost complete consensus" among parties that some kind of action must be taken. ISO-NE also notes that since the finding on New England's capacity market, the Commission has made a similar finding with regard to PJM's capacity market.

Commission Conclusion

99. We deny this request for rehearing. As noted above, at several points in the proceeding, we have addressed this argument and have reiterated our findings that the existing ICAP market is unjust and unreasonable.[113] Objecting Parties focus too narrowly on the Commission's determinations with regard to certain specific facilities that have applied for RMR contracts. As we stated in the June 16 Order, the increase in RMR agreements provides substantial evidence that signals a greater problem in the market, namely, its inability to compensate capacity resources needed to maintain the reliability

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[113] *Id.* at P 203, *citing* June 2 Order at P 29; April 25 Order at P 33, 37; July 24 Order at P 33.

of the system. Moreover, we note that in the June 16 Order, we pointed to substantial record evidence regarding the inability of generators to earn sufficient revenues in the current market, both to continue operating or to support new investment.[114] Objecting Parties do not contradict this evidence.

100. Objecting Parties claim that the existing ICAP market cannot be found unjust and unreasonable because there is currently a surplus of capacity, and because certain generators are earning sufficient revenues, are unavailing. Again, the Commission found the existing ICAP market unjust and unreasonable because it failed to sufficiently compensate generating units needed for reliability, particularly in constrained areas. The presence of a surplus region-wide or the existence of a few generators earning adequate revenues do not contradict or invalidate the unjust and unreasonable finding. Moreover, load in New England is growing, and the existing surplus is projected to disappear.[115]

(ii) **Commission Jurisdiction**

101. The Commission concluded in the June 16 Order that it has ample jurisdiction to consider and approve the Settlement Agreement. In particular, the Commission stated that the settlement does not alter the method by which resource adequacy determinations (particularly to determination of the installed capacity requirement) are made or direct that a particular amount of capacity be

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[114] *Id.* at P 204.

[115] According to ISO-NE's 2005 Annual Markets Report, "total system generation capacity did not change significantly during 2005, with a net increase of 11 MW." Peak demand has grown from 24,116 MW in 2004 to 28,127 MW in 2006.

installed.[116] Further, the Commission noted that the Settlement Agreement was "squarely within the Commission's jurisdiction under the FPA" because it establishes a mechanism and market structure for the purchase and sale of installed capacity at wholesale in interstate capacity and to determine the prices for such sales.[117] The Commission also pointed out that the Settlement Agreement permits parties to self-supply their capacity obligations.

Requests for Rehearing

102. Objecting Parties argue that the Settlement Agreement devises a scheme that is directed toward determining how much generation needs to be available to satisfy local load requirements and, as such, imposes a resources adequacy requirement upon utilities in the New England states, in contravention of the FPA. Objecting Parties assert that under the FPA the Commission has no legal authority to require that any utility purchase generation services or generation capacity, adding that section 201 of the FPA reserves to the states plenary authority over generation, including the determination of how much generation individual utilities must own or control to reliably serve retail customers. Objecting Parties add

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[116] June 16 Order at P 201.

[117] *Id.* The Commission noted that courts have confirmed the Commission's jurisdiction over the price of capacity in wholesale markets. *Id., citing Municipalities of Groton v. FERC*, 587 F.2d 1296 (D.C. Cir. 1978) (holding that the Commission had jurisdiction over the installed capability charge in New England, a precursor to ICAP); *Mississippi Industries v. FERC*, 808 F.2d 1525 (D.C. Cir. 1987) (holding that the Commission could exercise jurisdiction over the allocation of the costs of capacity among four utility operating companies of a holding company under "its undisputed authority over the wholesale rates of electric generating facilities in interstate commerce.").

that the June 16 Order did not discuss the recent Energy Policy Act of 2005, which further delineates the jurisdictional divide between FERC and the states with regard to electric system reliability. Objecting Parties argue that while Congress imposed requirements for a FERC-jurisdictional "reliability standard," the Act explicitly provides that this did not include requirements to enlarge facilities or to construct new transmission or generation capacity.

103. Objecting Parties also assert that the FPA does not confer upon the Commission the authority to approve prices for generation capacity. Objecting Parties reference certain Settlement Agreement provisions, including those governing the use of CONE, the collar mechanism and the payment schedule established to cover the transition period, arguing that these provisions will require participating load serving entities to pay dictated prices. Objecting Parties assert that the Settlement Agreement sets a specific payment schedule for all capacity in the transition. In reference to provisions that establish the beginning price for each FCA,[118] Objecting Parties state that the Settlement Agreement stipulates the price that will be paid to existing capacity and new capacity when the "collar" is triggered.[119]

104. Objecting Parties argue that participation in the FCM must be voluntary as the Commission lacks author-

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[118] The beginning price of the FCA shall have a starting price of 2 times CONE, with CONE initially set at $7.50/kW-month (therefore, the initial starting price will be $15). See Settlement Agreement at Section III.F.

[119] Until there have been three successful auctions, the price for existing capacity will be set within a ceiling of 1.4 times CONE and a floor of 0.6 times CONE, which is referred to as the "collar mechanism."

ity to mandate how a utility satisfies its reserve requirements. Objecting Parties contend that though a load-serving entity may choose to self-supply its capacity obligations this does not render the participation in the FCM voluntary. Objecting Parties further contend that the self-supply provision does not represent an "opt out" provision as resources designated as self-supply are subject to the same performance obligations and qualification requirements as other resources participating in the FCM and the Forward Capacity Auctions.

Answers

105. NEPOOL asserts that the Commission has previously considered and rejected the jurisdictional arguments raised by the Objecting Parties, and that Objecting Parties offer no new legal or factual arguments that the Commission has not previously considered. In particular, NEPOOL notes that the Commission rejected similar jurisdictional arguments in a November 8, 2004 Order in this docket.[120]

106. NEPOOL contends that Objecting Parties' jurisdictional objections are related to responsibility for establishing the Installed Capacity Requirement (ICR).[121] NEPOOL states that, historically, establishment of the ICR level was the responsibility of NEPOOL, not any state regulator. With ISO-NE becoming a regional transmission organization, responsibility for determining ICR shifted to ISO-NE. ISO-NE's determination is presented to NEPOOL for an advisory vote prior to filing

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[120] *Devon Power LLC*, 109 FERC ¶ 61,154.

[121] The ICR is the level of capacity required to meet the reliability requirements defined for the New England control area; the ICR determines how much capacity will be bought through capacity auctions. ISO-NE calculates the ICR annually.

with the Commission. NEPOOL states that the Settlement Agreement does not modify tariff provisions that govern the process for determining ICR. Moreover, NEPOOL states that the Commission rejected the Objecting Parties' jurisdictional arguments when it approved the ISO-NE's proposed ICR values for the 2005/2006 Power Year.[122]

107. ISO-NE argues that the Commission correctly held that it has jurisdiction to approve the Settlement Agreement and states that no new arguments have been raised on rehearing. ISO-NE notes that this issue was extensively discussed in the LICAP proceeding and in Docket No. ER05-715-000.[123] Finally, ISO-NE states that the issue of the ISO's authority to file a proposed installed capacity requirement, as well as the Commission's jurisdiction to approve it, is currently before the United States Court of Appeals for the District of Columbia Circuit[124] and thus needs no further elaboration here.

Commission Conclusion

108. The Commission denies Objecting Parties' request for rehearing with regard to jurisdiction. Objecting Parties have presented few new arguments that the Commission has not already addressed in this proceeding. As we concluded in the June 16 Order, courts have unequivocally confirmed that the Commission has jurisdiction under the FPA to regulate the charges for capacity in

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[122] *ISO New England, Inc.*, 111 FERC ¶ 61,185, *reh'g denied*, 112 FERC ¶ 61,254 (2005), *appeal docketed Connecticut Department of Public Utility Control v. FERC*, No. 05-1411 (D.C. Cir. filed Oct. 28, 2005).

[123] On March 21, 2005, ISO-NE filed materials, which identify the monthly Installed Capacity Requirements established by the ISO for the 2005/2006 power year.

[124] *See supra* note 122.

wholesale markets.[125] As we discussed in the June 16 Order, FCM only establishes a market design for determining capacity charges; it does not alter ICR or in any way determine the appropriate amount of capacity that must be available. As many of the parties here note, the issue of the Commission's jurisdiction over ICR is the subject of other proceedings and is outside the scope of this case.

109. The Commission's authority in EPAct 2005[126] over bulk electric system reliability is irrelevant in this proceeding. The Commission is not operating under that authority in this case, and as a result, there is no need to discuss it here.

110. Objecting Parties still do not explain why they believe the FCM system is mandatory when there is a self-supply option.[127] Furthermore, the performance obligations for capacity resources (including those self-supplied) noted by Objecting Parties have no bearing on whether the Commission, by approving FCM, is mandating the procurement of a certain level of generation capacity, the issue raised here. Those performance obligations are included in FCM to ensure that capacity resources are available when needed. They do not re-

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[125] June 16 Order at P 201, *citing Municipalities of Groton v. FERC*, 587 F.2d 1296 (D.C. Cir. 1978) (holding that the Commission had jurisdiction over the installed capability charge in New England, a precursor to ICAP); *Mississippi Industries v. FERC*, 808 F.2d 1525 (D.C. Cir. 1987) (holding that the Commission could exercise jurisdiction over the allocation of the costs of capacity among four utility operating companies of a holding company under "its undisputed authority over the wholesale rates of electric generating facilities in interstate commerce.").

[126] Energy Policy Act of 2005, Pub. L. No. 109-58, § 1236, 119 Stat. 961 (2005).

[127] June 16 Order at P 201.

quire that a specific level of generation be procured or infringe on the states' traditional role in determining resource adequacy requirements, as Objecting Parties suggest.

111. In approving CONE, the Commission is not approving prices for generation capacity. Prices for capacity will be established via descending clock auctions, and thus will ultimately be established via competitive bidding. CONE represents the estimated cost of new entry ($7.50/kw-month) and serves as the basis for the beginning point for the first FCA. Settling Parties agreed on a beginning point for the first FCA: 2 times CONE. In order to hold an FCA, a beginning point must be determined. As the proponents of a New England Resource Adequacy Market (a similar design that was proposed at the oral argument in this proceeding) stated in pre-oral argument briefs:

> Under the descending clock auction, the auctioneer (*e.g.*, ISO) will announce a price that is high enough to induce potential new entrants to participate. Potential entrants, existing generators, and load (for demand response mechanisms) would respond by offering to provide capacity at the specified price, assuming that the price is high enough to induce more supply than required.[128]

Commission approval of this reasonable beginning point for the FCAs does not constitute approval of generation prices. Moreover, we note that, following the first FCA, CONE will be "calculated using the clearing prices of

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[128] Statement in Support of the New England Resource Adequacy Market of the NERAM Proponents, filed in Docket No. ER03-563-030 September 13, 2005.

previous auctions"[129] and thus will rely on competitive prices.

112. The collar mechanism will apply in a limited number of FCAs and will only apply to existing resources. The collar mechanism represents a tool designed to ensure that capacity resources materialize in the first FCAs, thereby minimizing the risk of auction failure and ensuring the long-term viability of the FCM. In this regard, it is a component of a just and reasonable package of reforms. Moreover, the Commission also notes that there is no guarantee that it will be triggered during the initial FCAs. Regardless, as discussed above and in the June 16 Order, the Commission has ample authority under the FPA to regulate the charges for capacity in the wholesale markets.[130]

(iii) Incentive Rates

Requests for Rehearing

113. Objecting Parties assert that the Commission erred in providing incentive rates to existing generators. Objecting Parties assert that under the Settlement Agreement, all existing capacity resources would be paid capacity payments with no incentive to build new capacity. Objecting Parties contend that the Settlement Agreement fails to demonstrate a connection between paying incentive-based capacity payments to existing resources and increases in installed capacity. Objecting Parties contend that the just and reasonable standard

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[129] See Explanatory Statement of the Settling Parties in Support of the Settlement Agreement at 26, filed March 6, 2006.

[130] *See also* 16 U.S.C. § 824(b)(1) (2000) ("The provisions of this Part shall apply to the transmission of electric energy in interstate commerce and the sale of electric energy at wholesale in interstate commerce.").

historically has required that incentive rates be restricted to those responding to the incentive. Objecting Parties contend that owners of existing generation resources will have little incentive to add capacity because the new capacity will reduce revenues to their existing resources.

Answers

114. ISO-NE argues that capacity payments to existing generators are not incentive rates but are market rates missing from the current capacity market and that these missing revenues are the reason that the Commission ordered a market-based mechanism be implemented. ISO-NE further argues that this argument was already addressed and rejected by the United States Court of Appeals for the District of Columbia Circuit.[131] In that appeal, ISO-NE states that the court rejected ELCON's argument that a heightened standard of review should be applied as NYISO's ICAP market granted a windfall to existing capacity suppliers at the expense of load serving entities and their customers.

Commission Conclusion

115. We deny this request for rehearing as well. Previously in this proceeding, the Commission fully addressed and dismissed arguments that a capacity market mechanism provided "incentive rates" and thus required that the Commission use a different standard for approval. In particular, in a November 8, 2004 Order on Rehearing and Clarification,[132] the Commission addressed an argument by the NEPOOL Industrial Consumer Coalition (NICC) that federal case law regarding the Commission's incentive ratemaking authority applied to the Commis-

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[131] *Electricity Consumers Resource Council*, 407 F.3d 1232 (D.C. Cir. 2005) (*ELCON*).

[132] *Devon Power LLC*, 109 FERC ¶ 61,154 at P 43-44 (2004).

sion's consideration of the LICAP mechanism. NICC argued that LICAP amounted to an incentive rate scheme, and as a result, the Commission was required under case law to demonstrate that it is "reasonably calculated to achieve a specific policy objective," and required the Commission to ensure that any rate increases used to achieve the policy goals of LICAP were "'in fact needed, and . . . no more than needed.'"[133] The Commission concluded that the LICAP mechanism was not an incentive ratemaking proposal because it was not a rate structure designed to provide direct incentives aimed at increasing energy supplies by increasing prices.[134] Instead, the Commission stated that the proposal (when finalized) would produce just and reasonable rates for capacity, and would reduce volatility of ICAP prices, which both would provide a natural incentive to build capacity where needed. The Commission held that this fact distinguished the LICAP mechanism from the incentive rate proposals approved by the Commission and considered by the courts in the cases holding that a different demonstration must be made to approve such proposals.[135]

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[133] *See* Request for Rehearing of NICC in Docket Nos. ER03-563-038 and EL04-102-001at 15-16, *citing Pub. Service Comm'n of the State of New York v. FERC*, 589 F.2d 542 (D.C. Cir. 1978) and *City of Detroit v. FPC*, 230 F.2d 810, 817 (D.C. Cir. 1955). NICC also cited the following cases: *City of Charlottesville v. FERC*, 661 F.2d 945 (D.C. Cir. 1981); *Farmers Union Cent. Exch., Inc. v. FERC*, 734 F.2d 1486 (D.C. Cir. 1984); *Pub. Util. Comm'n of the State of California v. FERC*, 367 F.3d 925 (D.C. Cir. 2004). *See also ELCON*, *supra* note 131.

[134] *Devon Power LLC*, 109 FERC ¶ 61,154 at P 44.

[135] *Id.*, *citing Pub. Service Comm'n of the State of New York v. FERC*, 589 F.2d 542; *City of Charlottesville v. FERC*, 661 F.2d 945; *Farmers Union Cent. Exch., Inc. v. FERC*, 734 F.2d 1486; *Pub. Util. Comm'n of the State of California v. FERC*, 367 F.3d 925.

116. While the Settlement Agreement adopts a different structure for the capacity market, our earlier conclusion holds. The FCM, like LICAP, is designed to establish just and reasonable rates for capacity and stabilize those rates over time. It does not, either through the transition payments or the FCAs, provide direct incentives aimed at increasing energy supplies by increasing prices. Since our earlier ruling on this issue, in *ELCON*, the court upheld New York's capacity market design against a challenge that it constituted incentive ratemaking for these same reasons.[136] While the FCM will, we believe, provide an incentive for the addition of significant new capacity, this incentive is the natural outgrowth of just and reasonable compensation for capacity resources, which has been missing from New England's capacity market for several years. Because FCM does not provide any direct increased payments directed exclusively to increasing supplies, the incentive ratemaking cases are inapplicable here.

8. Motion for Clarification

117. Maine Parties ask that the Commission clarify that ISO-NE will account for export-constraints as part of the auction process. Section III.A.5 of the Settlement Agreement states that export-constrained zones are modeled in the forward capacity auctions. Maine Parties refer to reply comments filed by ISO-NE, which confirmed that export constraints will be modeled in the auction,[137] stating that the Commission noted the same comments in the FCM Order without requiring the ISO to model export constraints through the auction. Maine Parties believe that modeling exports through the auc-

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[136] 407 F.3d at 1237-38.

[137] Reply Comments Regarding Settlement Agreement of ISO-NE at 43 (filed April 5, 2006).

tion is critical to the functions of the capacity markets and request that the Commission clarify that the ISO should model export constraints in the auction.

Answers

118. In response, ISO-NE states that it does not object to the requested clarification. ISO-NE asserts that it will model the constraints before the auction and that the auction itself will determine whether the constraints will bind so as to establish separate capacity zones.

Commission Conclusion

119. We grant Maine Parties' request for clarification that the ISO should model export constraints in the auction. Section III.A.5 of the settlement explicitly states: "Export-constrained zones are modeled in the FCA."

The Commission orders:

(A) The requests for rehearing are hereby denied, as discussed in the body of this order.

(B) The request for clarification is hereby granted, as discussed in the body of this order.

By the Commission. Commissioner Kelly concurring with a separate statement attached.

Commissioner Wellinghoff concurring with a separate statement attached.

(SEAL)

Magalie R. Salas,
Secretary.

Appendix A – List of Settling Parties

American National Power, Inc.
Associated Industries of Massachusetts
Boston Generating, LLC
Calpine Eastern Corporation
Calpine Energy Services, L.P.
Cape Wind Associates, LLC
Central Vermont Public Service Corporation
Connecticut Department of Public Utility Control
The Connecticut Light and Power Company
Connecticut Municipal Electric Energy Cooperative
Connecticut Office of Consumer Counsel
Conservation Services Group
Consolidated Edison Energy, Inc.
Dominion Energy Marketing, Inc.
Dominion Nuclear Connecticut, Inc.
Dominion Resources, Inc.
Duke Energy North America, LLC
Energy Management, Inc.
EnerNOC, Inc.
Entergy Nuclear Generation Company
Entergy Nuclear Vermont Yankee, LLC
Exelon Generation Company, LLC
Exelon New England Holdings, LLC
Fitchburg Gas & Electric Light Company
FPL Energy, LLC
Granite Ridge Energy, LLC
HQ Energy Services (U.S.), Inc.
ISO New England, Inc.
Lake Road Generating Company, LP

Long Island Power Authority (LIPA)

MASSPOWER

Milford Power Company, LLC

Mirant Americas Energy Marketing, LP

Mirant Canal, LLC

Mirant Kendall, LLC

Mystic Development, LLC, Mystic I, LLC. and Fore River Development, LLC

National Grid USA (on behalf of itself and its subsidiaries that are intervenors in this proceeding)

NEPOOL Participants Committee

New Hampshire Electric Cooperative, Inc.

New Hampshire Office of Consumer Advocate

New Hampshire Public Utilities Commission

NRG (Devon Power, LLC. Middletown Power LLC, Montville Power LLC, Norwalk Harbor, LLC, and NRG Power Marketing)

Pinpoint Power

Public Service Company of New Hampshire

RI Division of Public Utilities and Carriers

RI Public Utilities Commission

Select Energy

Sempra Trading

TransCanada Power Marketing Limited

The United Illuminating Company

Vermont Department of Public Service

Vermont Public Power Supply Authority

Vermont Public Service Board

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Devon Power LLC Docket No. ER03-563-060

(Issued October 31, 2006)

KELLY, Commissioner, *concurring*:

I agree with Industrial Energy Consumers Group that the Commission should not apply the *Mobile-Sierra* "public interest" standard with respect to generally-applicable market rules and tariffs. For the reasons set forth in my concurring statement on the June 16, 2006 order in this proceeding, and as further explained below, I believe that the *Mobile-Sierra* "public interest" standard provision is acceptable in this case.

Section 4.C.i of the settlement applies the *Mobile-Sierra* "public interest" standard with respect to challenges to the final capacity clearing prices and prices resulting from reconfiguration auctions and the market rules related to this provision after they are approved by the Commission. As stated in this order, the Commission will review the final auction clearing prices before they are finalized. ISO-NE will need to make an informational filing prior to each auction that includes information about the zones to be used and qualifying bids, and then make a filing under FPA section 205 after each auction containing the results. These filings will be reviewed under the FPA's "just and reasonable" standard. In addition, these prices will be in place for a time-limited period, as they will be replaced each year by the subsequent FCM auctions.

In addition, Section 4.C.ii applies the *Mobile-Sierra* "public interest" standard with respect to the transition mechanism and the market rules implementing that

mechanism. From December 1, 2006 until June 1, 2010, the settlement provides for a transition period during which fixed payments will be made to all installed capacity. These fixed payments are netted against RMR payments and reduced based on availability, and will terminate once the FCM is implemented.

As part of its rationale for accepting the *Mobile-Sierra* "public interest" provision in Section 4.C of the settlement, as it applies to the Commission acting *sua sponte* and on behalf of third parties, the order states that the Commission has "routinely" and "consistently" permitted the use of such provisions in recent orders. I wish to note that I have dissented from those orders on this point and continue to oppose the acceptance of such provisions, except in circumstances where the parties show that the Commission should approve their request for the higher "public interest" standard of review set forth in *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332 (1956) *(Mobile) and Federal Power Commission v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956) (*Sierra*).[1]

Therefore, although I disagree with some of the order's stated rationale for approving the *Mobile-Sierra* "public interest" standard provision specified in this settlement, I believe that the broad support among varied parties for the settlement and the constrained and time-limited application of the "public interest" standard in this case warrant approval of this order.

Suedeen G. Kelly

[1] *See Entergy Services, Inc.*, 117 FERC ¶ 61,055 (2006) (concurring statement).

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Devon Power LLC Docket No. ER03-563-060

(Issued October 31, 2006)

WELLINGHOFF, Commissioner, *concurring*:

In Section 4.C of the instant Settlement Agreement, the Settling Parties have asked the Commission to apply the "public interest" standard of review in narrow circumstances. Because the facts of this case satisfy the standards that I identified in *Entergy Services, Inc.*,[1] I believe that it is appropriate for the Commission to grant the parties' request and agree to apply the "public interest" standard in those narrow circumstances to future changes sought by a party, a non-party, or the Commission acting *sua sponte*. I write separately to explain my conclusion with regard to this issue.

As I stated in *Entergy*, where the parties to an agreement ask the Commission to apply the "public interest" standard to future changes sought by non-parties or the Commission acting *sua sponte*, I would require the parties to demonstrate by substantial evidence that a factual and policy basis supports their request. Elaborating on that requirement, I stated that the Commission should only grant such requests in narrowly proscribed circumstances where substantial evidence affirmatively demonstrates that the agreement at issue has broad-based benefits to both parties and non-parties. In making this assessment, I would take into consideration, among other issues: (1) whether the agreement was negotiated through a stakeholder process reflecting a wide range of

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[1] 117 FERC ¶ 61,055 (2006) (*Entergy*).

interests, (2) whether state commissions had meaningful opportunity to participate in the stakeholder process, (3) the extent of and justification for opposition to the request for the Commission to apply the "public interest" standard, and (4) whether granting the request is necessary to the resolution of the proceeding.

Applying these standards to the facts of this case, I believe that it is appropriate for the Commission to agree to apply the "public interest" standard in the narrow circumstances requested by the Settling Parties. First, substantial evidence in the record demonstrates that the Settlement Agreement has broad-based benefits to both parties and non-parties. The capacity problem in New England is well-documented, with flaws in the ICAP market first identified in 2000. Although a series of modifications to ISO-NE's ICAP mechanism were made over the ensuing years, capacity deficiency persisted and grew. For example, a total of 11 MW of regional electricity supply was added in New England in 2005. At the same time, peak demand rose by 2,700 MW.[2]

The Commission has repeatedly stated its concerns about this situation. In the order that initiated the negotiations that produced the Settlement Agreement, the Commission cited a general agreement among the parties that "the status quo is failing and that generation resources are not being added at a rate necessary to maintain reliability and assure just and reasonable wholesale power prices."[3] Similarly, in the order accepting the Settlement Agreement, the Commission found that while

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[2] *See* Statement of Chairman Joseph T. Kelliher at June 15, 2006 Open Commission Meeting (Docket No. ER03-563-055).

[3] *Devon Power LLC*, 115 FERC ¶ 61,340 at P 14 (2006) (June 16, 2006 Order), citing *Devon Power LLC*, 113 FERC ¶ 61,075 (2005). I note that both of these orders issued prior to my becoming a Commissioner.

New England has sufficient capacity to meet reliability requirements today, additional infrastructure is needed soon to avoid violations of reliability criteria.[4] The Commission also found that the Settlement Agreement provides necessary solutions to resolve these severe problems related to New England's infrastructure.

Second, the parties that participated in the underlying negotiations reflected a wide range of interests. As the Commission stated in its order accepting the Settlement Agreement, from October 2005 until March 2006, over 175 representatives – including representatives from the region's state public utility regulatory agencies, transmission owners, generators, power traders and marketers, demand response and intermittent resource owners, consumer-owned utility systems, and end users – engaged in informal and formal settlement negotiations.[5] While the negotiations did not result in unanimous support for their product, the Settlement Agreement drew support from a significant majority of the participating parties, including four state public service commissions.

Third, two parties (IECG and Maine Parties) sought rehearing of the Commission's refusal to modify or eliminate the application of the "public interest" standard under Section 4.C of the Settlement Agreement. Among other concerns, those parties argue that the proposed application of the "public interest" standard may prevent the Commission from taking appropriate steps in the future with regard to problems that may arise with the new market design. The Settlement Agreement, however, provides that ISO-NE will make filings with the Commission following the forward capacity auctions that reflect their results. Particularly because non-parties

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[4] June 16, 2006 Order at P 63.

[5] *Id.* at P 66.

will be able to challenge such filings under the "just and reasonable" standard, and the Commission will review such challenges under that same standard, I agree with the Commission that these required regular filings will reveal unanticipated problems with the new market design and provide an adequate opportunity to address them.

Another argument raised by parties seeking rehearing is that a settlement may not bind the Commission or non-parties to the "public interest" standard. As I stated in *Entergy and Enron Power Marketing, Inc.*,[6] the Commission has discretion to agree to apply the "public interest" standard to future changes sought by non-parties or the Commission acting *sua sponte*, and should exercise that discretion based on careful consideration of the interests of parties and non-parties. In light of the broad-based benefits to both parties and non-parties discussed above, and the other considerations discussed herein, I believe that it is appropriate for the Commission to agree to apply the "public interest" standard in the narrow circumstances requested by the Settling Parties.

For these reasons, I respectfully concur with the Commission's order.

Jon Wellinghoff
Commissioner

[6] 117 FERC ¶ 61,109 (2006).

APPENDIX C

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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115 FERC ¶ 61,340

Before Commissioners: Joseph T. Kelliher, Chairman; Nora Mead Brownell, and Suedeen G. Kelly

Devon Power LLC — Docket Nos. ER03-563-030, ER03-563-055

ORDER ACCEPTING PROPOSED SETTLEMENT AGREEMENT

(Issued June 16, 2006)

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1. In these proceedings, the Commission has been addressing a proposal by ISO New England, Inc. (ISO-NE) to establish a locational installed capacity (LICAP) mechanism. That proposal was made in response to Commission orders identifying flaws in New England's current capacity market, and was further developed through subsequent hearing procedures. As this proceeding has developed, additional evidence has been produced regarding the flaws in the current capacity market and the resulting impacts those flaws have had on New England's electric system infrastructure. As discussed in more detail below, the Commission established additional proce-

dures to consider how the LICAP mechanism would address the deficiencies in the current capacity market and meet New England's projected need for new infrastructure in coming years. Those additional procedures also gave the parties an opportunity to discuss and develop potential alternatives to the LICAP mechanism.

2. On March 6, 2006, a broad group of the parties to this proceeding (collectively Settling Parties[1]) filed a proposed settlement (Settlement Agreement) that would resolve all issues in this matter. As described in more detail in this order, the Settlement Agreement contains an alternative to LICAP, called the Forward Capacity Market (FCM). The settlement is contested. In this order, we accept the proposed Settlement Agreement, finding that as a package, it presents a just and reasonable outcome for this proceeding consistent with the public interest.

I. Background and Procedural History

3. The Initial Decision contains a detailed history of this proceeding up to the point of its issuance.[2] Rather than repeat that detailed history here, we will briefly recount certain key points of prior proceedings and the present case.

4. As a means of ensuring reliability, for many years ISO-NE (and previously NEPOOL) has imposed an installed capacity (ICAP) requirement on load-serving entities, requiring them to procure specified amounts of ICAP based on their peak loads plus a reserve margin. Prior to the widespread unbundling of the generation, transmission and distribution functions of most New

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[1] Settling Parties are identified in Appendix A to this order.

[2] *See Devon Power LLC*, 111 FERC ¶ 63,063 at P 2-36 (2005) (Initial Decision).

England load-serving entities (which in many cases included state-mandated divestiture of generating assets), if a utility did not have sufficient resources to meet its ICAP requirement, it could either obtain ICAP from an entity in the pool with a surplus or pay the deficiency charge.

5. Beginning in 1998, ISO-NE began operating a bid-based market for ICAP.[3] In 2000, as part of the region's development of wholesale power markets and market-based rates, the Commission first began to identify flaws in the ICAP market. In an order addressing competing proposals to implement a congestion management system and multi-settlement system in New England, the Commission rejected a proposal by ISO-NE to eliminate the ICAP requirement, reasoning that ISO-NE should first propose an alternative mechanism to meet the reliability function served by the ICAP requirement.[4] The Commission did allow ISO-NE to replace the ICAP auction mechanism with an administratively-determined ICAP deficiency charge, agreeing with ISO-NE that the auction "can produce inflated prices unrelated to the actual harm caused by ICAP deficiencies."[5]

6. In 2002, the Commission further addressed deficiencies in New England's ICAP market, this time noting the lack of a locational element. In its order addressing the implementation of energy markets and locational marginal pricing in New England, the Commission identified the lack of a locational element as a significant flaw in the ICAP market, stating that it "believes that location is an

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[3] *See New England Power Pool*, 83 FERC ¶ 61,045 at 61,263 (1998).

[4] *See ISO New England, Inc.*, 91 FERC ¶ 61,311 (2000).

[5] *Id.* at 62,081.

important aspect of ensuring optimal investment in resources."[6]

7. These specific proceedings began in response to the February 26, 2003 filing by Devon Power LLC, Middletown Power LLC, Montville Power LLC, Norwalk Power LLC and NRG Power Marketing Inc. (collectively NRG) of four cost-of-service reliability-must-run (RMR) agreements covering 1,728 megawatts of generating capacity located within Connecticut and the constrained Southwest Connecticut area. In a series of orders addressing NRG's filing[7] as well as RMR agreements filed by other entities,[8] the Commission rejected the majority of the RMR agreements, out of concern about the effect widespread use of such contracts could have on the competitive market. The Commission stated that ISO-NE, "rather than focusing on and using stand-alone RMR agreements, should incorporate the effect of those agreements into a market-type mechanism."[9] Accordingly, the Commission directed, pursuant to section 206 of the Federal Power Act (FPA),[10] that revised bidding rules (called Peaking Unit Safe Harbor, or PUSH, bidding) be instituted on an interim basis to give low-capacity factor generating units operating in designated congestion areas the opportunity to recover their costs through the market.[11] To replace the interim PUSH mechanism, the

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[6] *New England Power Pool and ISO New England, Inc.*, 100 FERC ¶ 61,287 at 62,278 (2002).

[7] *Devon Power LLC*, 102 FERC ¶ 61,314 (2003) (March 25 Order); *Devon Power LLC*, 103 FERC ¶ 61,082 (2003) (April 25 Order); *Devon Power Company*, 104 FERC ¶ 61,123 (July 24 Order).

[8] *PPL Wallingford Energy LLC*, 103 FERC ¶ 61,185 (2003); *PPL Wallingford Energy LLC*, 105 FERC ¶ 61,324 (2003).

[9] *See* April 25 Order at P 29.

[10] 16 U.S.C. 824e (2000).

[11] *See* April 25 Order at P 33; July 24 Order at P 25-31.

Commission directed ISO-NE to file by March 1, 2004, for implementation by June 1, 2004, "a mechanism that implements location or deliverability requirements in the ICAP or resource adequacy market ... so that capacity within [designated congestion areas] may be appropriately compensated for reliability."[12]

8. On March 1, 2004, ISO-NE made its filing in compliance with the April 25 Order. In the compliance filing, ISO-NE proposed a locational installed capacity (LICAP) mechanism that would add a locational element to the current ICAP market, establishing four ICAP regions with separate ICAP requirements: Maine, Connecticut, Northeast Massachusetts/Boston (NEMA/Boston), and the remainder of New England (Rest of Pool). Under the proposal, capacity transfer limits would be established to limit the amount of ICAP that load serving entities in one region could purchase from another region. Additionally, ISO-NE proposed to use a downward sloping demand curve to establish the amount of ICAP which must be procured and the price for that capacity. Additionally, under the proposed LICAP mechanism, capacity transfer rights would be allocated to load or generators, depending on their location, to allow market participants to hedge against congestion costs. Under the proposal, holders of capacity transfer rights between two ICAP regions would receive the difference in ICAP prices between those regions.

9. In a June 2, 2004 Order,[13] the Commission established hearing procedures regarding ISO-NE's compliance filing, and delayed the implementation of the LICAP mechanism from the proposed June 1, 2004 date until January 1, 2006. The Commission stated that it agreed with

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[12] April 25 Order at P 37.

[13] *Devon Power LLC*, 107 FERC ¶ 61,240 (2004) (June 2 Order).

two broad concepts in ISO-NE's proposal. First, the Commission found it appropriate to establish separate ICAP regions, but questioned whether the regions proposed by ISO-NE adequately reflected where infrastructure investment is needed most, specifically noting the constrained area of Southwest Connecticut. Second, the Commission agreed with the overarching concept of a demand curve, but found that more information was necessary to develop appropriate parameters for the curve. As a result of these findings, the Commission directed ISO-NE to submit a further filing addressing whether the Commission should revise the LICAP proposal to create a separate ICAP region for Southwest Connecticut. Additionally, the Commission established a separate investigation and paper hearing in Docket No. EL04-102-000 to determine whether a separate energy load zone should be created for Southwest Connecticut, and whether it should be implemented in advance of LICAP. Finally, the Commission established hearing procedures to determine the appropriate demand curve parameters, the proper method for calculating capacity transfer limits, the appropriate method for determining the amount of capacity transfer rights to be allocated, and the proper allocation of capacity transfer rights. In subsequent orders, the Commission addressed ISO-NE's filing regarding the creation of a separate ICAP region for Southwest Connecticut, and denied rehearing and granted clarification in part of the June 2 Order.[14]

10. On June 15, 2005, the Presiding Judge issued an Initial Decision on the issues set for hearing in the June 2

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[14] *See* June 2 Order, *order on reh'g and clarification, Devon Power LLC*, 109 FERC ¶ 61,154 (2004), *reh'g denied*, 110 FERC ¶ 61,315 (2005); *see also Devon Power LLC*, 109 FERC ¶ 61,156 (order on compliance filing directing establishment of Southwest Connecticut region), *order on reh'g and clarification*, 110 FERC ¶ 61,313.

Order.[15] The Initial Decision largely (with some variation) adopted the demand curve proposed by ISO-NE in its August 31, 2004 initial testimony, and also ruled on the appropriate allocation of capacity transfer rights and the appropriate methodology for calculating capacity transfer limits. Briefs on Exceptions to the Initial Decision were filed on July 15, 2005, and Briefs Opposing Exceptions were filed on August 4, 2005.

11. In section 1236 of the Energy Policy Act of 2005, signed into law on August 8, 2005, Congress noted the New England Governors' concerns that the LICAP proposal would not provide adequate capacity or reliability while imposing high costs on consumers.[16] Congress declared that the Commission should carefully consider the states' objections.

12. Several entities (mostly state entities and load representatives) requested oral argument before the Commission on the exceptions to the Initial Decision, pursuant to Rule 711(c) of the Commission's Rules of Practice and Procedure.[17] In an August 10, 2005 Order, the Commission granted these requests and scheduled oral argument for September 20, 2005.[18] Additionally, the Commission stated that, in light of its decision to hear oral arguments, "we have determined that the implementation of the LICAP mechanism, if it proceeds, will not be earlier than October 1, 2006."[19]

13. The oral argument focused on whether the LICAP mechanism, as adopted in the Initial Decision, or any al-

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[15] *See supra* note 2.

[16] Pub. L. No. 109-58, § 1236, 119 Stat. 961 (2005).

[17] 18 C.F.R. § 385.711(c) (2005).

[18] *Devon Power LLC*, 113 FERC ¶ 61,075 (2005).

[19] *Id.* at P 5.

ternative approach would provide for just and reasonable wholesale power prices in New England, at levels that encourage needed generation additions and whether LICAP or any alternative approach would provide adequate assurance that necessary electric generation capacity or reliability will be provided. The Commission also asked the parties to address at oral argument what are the costs, benefits, and economic impacts of the proposal (or any alternative approach), compared to continued reliance on the status quo, such as the cost of RMR agreements. Both at the oral argument and in briefs filed prior to the oral argument, parties to the proceeding were given the opportunity to present alternatives to LICAP directly to the Commission.[20] Parties presented two alternatives to LICAP in their briefs and at oral argument: the New England Resource Adequacy Market and the New England Locational Resource Adequacy Market.

14. Following the oral argument, the Commission issued an order giving the parties an additional opportunity to pursue a settlement on an alternative to the LICAP mechanism.[21] In that order, the Commission stated that it remained concerned about the resource adequacy situation in New England (particularly in the congested areas of Southwest Connecticut and Northeastern Massachusetts), noting that "[t]he parties at the oral argument generally agreed that the status quo is failing and that generation resources are not being added at a rate necessary to maintain reliability and assure just and reasonable wholesale power prices."[22] The Commission

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[20] *See* Notice Scheduling Oral Argument, Docket No. ER03-563-030 (August 25, 2005).

[21] *Devon Power LLC*, 113 FERC ¶ 61,075 (2005) (October 21 Order).

[22] *Id.* at P 5.

directed the Chief Administrative Law Judge to appoint a settlement judge to guide the process of developing a proposed alternative to LICAP. Additionally, the Commission stated that it would continue to evaluate the Initial Decision, and directed ISO-NE to make a compliance filing to aid in its consideration of the Initial Decision.[23]

II. Description of Proposed Settlement Agreement

A. Forward Capacity Market

15. The Settlement Agreement provides for the implementation of an FCM as an alternative to the ISO-NE-designed LICAP mechanism. The Settlement Agreement is the end product of a series of over 30 formal settlement conferences that occurred over a four-month period with the active participation and involvement of Administrative Law Judge Lawrence Brenner. Of 115 parties to the settlement proceedings, eight parties have formally opposed the Settlement Agreement. The NEPOOL Participants Committee voted, with 78.46 percent, to support the Settlement Agreement, with support from all six voting sectors.

16. The FCM establishes annual auctions for capacity. The capacity product will be sold on a per-megawatt of deliverable capacity basis. Capacity resources, regardless of type, will receive the same auction clearing price. The Forward Capacity Auctions (FCA) will procure capacity three-plus years ahead of the commitment period, which is intended to provide for a planning period for new entry and allow potential new capacity to compete in the auctions. The commitment period is a year-long peri-

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[23] *Id.* at P 10-14.

od that corresponds to the ISO-NE power year.[24] Thus, sellers will commit to provide capacity for one year—for example, June 1, 2011 to May 31, 2012—three-plus years in advance of the commitment period. However, the Settlement Agreement grants new capacity the option to lock-in capacity prices for up to five years. New capacity may, during the process to qualify as an eligible resource, select a commitment period of up to five years, in one-year increments, provided that the resource meets certain auction criteria. This design element is intended to provide predictable revenues and facilitate financing for new capacity.

17. The FCAs are designed as descending clock auctions. In such an auction, the administrator announces a starting price. Bidding in the FCA will begin at a specified price—two times the agreed Cost of New Entry (CONE).[25]

18. Following the first auction, subsequent CONEs will be mathematically established, based on preceding CONEs and the clearing price of the preceding auction. The proposed FCM provides annual reconfiguration auctions to be held two and a half years prior to each commitment period, as well as twice-yearly seasonal auctions and monthly auctions just prior to, and during each commitment period. These reconfiguration auctions provide for the buying, selling and exchange of capacity obligations and maintenance of liquidity. There are three types of reconfiguration auctions: (i) three annual auctions (for trading year-long commitments) before the

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[24] The ISO-NE power year is a period of twelve months beginning June 1 of each year and ending on May 31 of the next calendar year.

[25] CONE, which represents the initial price of each auction, is set for the initial auction at $7.50/kW-month, which was negotiated as part of the settlement.

relevant commitment period, (ii) monthly auctions held prior to each commitment month, and (iii) seasonal auctions held prior to June and October of each year to accommodate transactions to sell a seasonal strip product. The reconfiguration auctions will preserve the locational element of the initial auction.[26]

19. Until there have been three successful auctions, the price for existing capacity will be set within a ceiling of 1.4 times CONE and a floor of 0.6 times CONE, which is referred to as the "collar mechanism." In the auctions to which the collar mechanism applies, if the auction clearing price is greater than 1.4 times CONE, existing capacity will be paid 1.4 times CONE and new capacity will be paid the auction clearing price. The auction clearing price will not fall below 0.6 times CONE. In the first year, this means that auction prices for existing capacity can range from $4.50 to $10.50/kW-month.

20. The amount of capacity procured will be that amount required to maintain the installed capacity requirement. Thus, if the system has surplus capacity, not all capacity resources offered will be purchased.[27] Each load-serving entity, as the ultimate purchaser of capacity, is required to pay for a share of the installed capacity requirement proportionate to its share of peak load. FCM allows load-serving entities to self-supply: load-serving entities may use owned and contracted resources (in whole or in part) to supply their capacity obligations. Thus a load-serving entity can meet its capacity obligations without paying the auction clearing price. Resources designated as self-supply are subject to the same performance obligations

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[26] The locational element of the FCM is described below.

[27] This component of the FCM differs from the LICAP proposal, which set a target level of capacity in excess of the installed capacity requirement.

and qualification requirements as other resources participating in the FCM and the FCAs.

21. Resources participating in the auctions will be designated as existing or new resources. Existing capacity will be defined as a resource previously listed as a resource in New England's capacity market; new capacity will never have been listed as a capacity resource. Existing capacity may also qualify as new capacity if it undertakes specified types of major investments to upgrade its facilities. The incremental amount of an increase in output from an existing capacity resource will be considered new capacity, provided the output increase is greater than or equal to two percent of the Resource's Summer Seasonal Claimed Capability. The Settlement Agreement indicates that additional thresholds for new capacity may be addressed in the stakeholder process, which will enable consultation from state utility regulatory agencies. The Settlement Agreement sets rules under which imported capacity is included in the FCAs.

22. Capacity resources, existing and new, are required to submit qualification documentation to be eligible to participate in the auctions. New capacity that is selected to provide capacity in the future must demonstrate control over the proposed project site, a critical path schedule with milestones supporting the feasibility of the project, and an interconnection analysis showing the impact of connecting to the transmission grid. The FCM proposal also enables bidding by demand-side and intermittent resources.

23. The FCM proposal contains a locational component. Before each auction, ISO-NE will determine capacity zones based on an identification of transmission limits that may bind. In instances where transmission limits are expected to bind (accounting for predicted upgrades that will be on-line by the commitment period), ISO-NE

will designate separate capacity zones and hold separate but simultaneous auctions.

24. Capacity suppliers will have their monthly capacity payments reduced to account for two phenomena. First a "peak energy rent" sum will be deducted from monthly capacity payments. The peak energy rent sum, originally developed in the LICAP proposal, is based on revenues that would be earned in the energy market by a hypothetical, proxy peaking unit. There are a number of agreed characteristics that apply to the hypothetical unit, including indexing to the marginal fuel. The peak energy rent deduction is designed as a hedge for load against price spikes in the energy market.

25. Suppliers will also have payments reduced to account for availability during designated periods of system stress (*i.e.*, Shortage Events). This provision is intended to create an economic incentive for capacity resources to be available when capacity is most valuable to load. Penalties will be assessed to suppliers for failing to be available during a Shortage Event and will be assessed on a resource-specific basis. On any critical day, a resource can have compensation reduced by up to 10 percent of annual auction payments if it is not available; in any month, a resource can lose up to two and one-half months of its annual FCA Payment.

26. The availability component of the FCM proposal also has a provision that expels capacity resources that perform poorly for an extended period, until availability improves. Prior to clearing a unit to participate in the FCA, ISO-NE will determine whether the resource meets two criteria: 1) in any four-year period, was the resource available during less than 40 percent of the Shortage Events; and 2) did the resource fail to be available for ten or more Shortage Events during the four-year period? If both of these criteria are met, the resource will not be

eligible to participate in the FCA. Until the resource achieves an availability score of 60 percent or higher in three consecutive years or has demonstrated to the satisfaction of ISO-NE that the source of the inadequate availability score has been remedied, it will remain ineligible.

27. The FCM contains several rules to address high concentrations of market power, whether held by buyers or sellers. First, the FCM proposes a set of auction rules that curb incentives to manipulate the market and distort capacity prices. Only specified types of bids are eligible to set the capacity clearing price. To ensure that the FCA clearing prices are determined competitively, the FCM is designed to allow new capacity to set the clearing price, thus providing a market-based measure of the cost of new entry. In addition, the FCM has specific market rules that declare the auction to possess insufficient competition, as well as provisions for setting the clearing price under such conditions. If the insufficient competition rule is triggered, new capacity resources are paid the capacity clearing price; existing capacity resources are paid the lower of the capacity clearing price or 1.1 times CONE.

28. Second, the Market Monitor will review bids priced above or below specified price thresholds, which are tied to percentages of CONE. For example, the Market Monitor will review and decide whether to accept into the auction a capacity resource that submits any type of delist bid (*i.e.*, enabling it to exit the market temporarily or shut down permanently) that is higher than 0.8 times CONE. In such instances, should the Market Monitor determine that the bid is consistent with the resource's net risk-adjusted going-forward and opportunity costs, the bid is incorporated into the auction. In addition, the Market Monitor will review any new capacity or im-

ported capacity bid below 0.75 times CONE, to determine whether the bids are consistent with the long run average costs of that new capacity resource or the opportunity cost (or another reasonable economic measure) for the import.

29. Third, the peak energy rent deduction is intended to help mitigate incentives to create price spikes in the energy market. Settling Parties assert that, while it may be profitable to raise prices in the energy market, the peak energy rent mechanism will remove any profits gained from the rise in prices because the extra revenues earned in the energy market are deducted from capacity payments.

B. Transition Period

30. June 1, 2010 is identified as the first period for which suppliers would receive payments pursuant to the FCA auction mechanism. The Settlement Agreement provides for a transition period—beginning December 1, 2006, ending June 1, 2010—during which, fixed payments will be made to all installed capacity. Below is a table that details the level of the payment as it increases over time during the transition period:

Transition Payments

Period	Payment ($/kW-month)
December 1, 2006 - May 31, 2007	$3.05
June 1, 2007 – May 31, 2008	$3.05
June 1, 2008 – May 31, 2009	$3.75
June 1, 2009 – May 31, 2010	$4.10

Transition payments will be netted against RMR payments and will be considered capacity payments for the purposes of netting in the locational forward reserves market. Settling parties state that no new compensation mechanism has been implemented and, to date, little new generation has been constructed in New England. Settling parties assert that such transition payments serve as a bridge to the implementation of the FCM and as a means to help ensure that existing generators remain available until new resources can be built. There is no locational component to the transition payments, meaning that suppliers in historically constrained regions of New England will receive the same per kW-month payments as suppliers in historically unconstrained regions.

31. Transition payments will be made by unforced capacity (UCAP) obligation holders (load-serving entities). UCAP obligations are determined by ISO-NE and are calculated as the load-serving entity's customers' proportionate share of peak load. Transition payments will be adjusted to account for unit availability. During the 3 1/2 year transition period, transition payments will be adjusted downward according to a modified equivalent demand forced outage rate (EFORd) measurement, which most heavily weights availability during times of greatest need.[28]

32. The currently applicable RMR agreements in New England are scheduled to terminate upon the implementation or effectiveness of a locational ICAP mechanism. The Settlement Agreement explicitly states that the beginning of the first commitment period (June 1, 2010) will be considered to be the implementation or effectiveness of a locational ICAP mechanism rather than the

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[28] EFORd measures the portion of time a unit is in demand, but is unavailable due to forced outages.

transition period. The Settlement Agreement states that nothing prejudices the rights of any party to challenge, seek to terminate or support an RMR agreement on any other grounds or restrict any party's rights to seek, agree to or oppose any RMR modifications.

33. The Settlement Agreement outlines processes to implement the transition period and FCM following approval by the Commission. Market rules governing the FCM will be developed in detail and filed with the Commission in at least two packages. The first filing, tentatively planned by October 1, 2006, will include rules for implementing the transition provisions on December 1, 2006. The second filing, which must be made by February 15, 2007, will contain the rules for the FCM. The Settlement Agreement provides that market rules will be developed in accordance with NEPOOL's traditional rule review process and will include the opportunity for input from state utility regulators. Parties to the settlement may challenge the market rules only on the grounds that they are inconsistent with, or not necessitated by, the Settlement Agreement.

C. Other Features

34. A critical input into the FCM will be the determination of the installed capacity requirement, which will determine how much capacity will be purchased through the auctions. The Settlement Agreement establishes a general timeline for determining the installed capacity requirement. ISO-NE is currently conducting a stakeholder process to review the process for deriving the installed capacity requirement. ISO-NE hopes to conclude that stakeholder process during the third quarter of 2006 and file a revised process with the Commission, in the latter part of 2006. Based upon the outcome of that filing, the installed capacity requirement for the first auction will be filed during the third quarter of 2007, with

a requested effective date of October 1, 2007, enabling the first auction to be conducted no later than early 2008.

35. Settling Parties waive their rights under section 206 of the FPA to seek a change in the Settlement Agreement or the market rules implementing the agreement for the period beginning March 6, 2006 through the earlier of September 5, 2008 or the date on which the prices from the second FCA become final (roughly 2 1/2 years). During this period, ISO-NE will retain its authority under section 205 of the FPA (subject to appropriate stakeholder processes) to file modifications of the market rules that address the terms of the Settlement Agreement. ISO-NE may exercise that authority only where it can demonstrate that failure to implement the proposed change would have a negative effect on 1) system reliability or security, or 2) the competitiveness or efficiency of the forward capacity or forward reserve markets. Were ISO-NE to make such a filing, Settling Parties will retain all of their rights to challenge the proposed modifications before the Commission.

36. The Settlement Agreement states that final prices derived from all auctions and the transition provisions cannot be changed unless required by the public interest under the *Mobile-Sierra* standard.[29] Settling parties assert that one reason for adopting this standard for final auction prices is to reduce regulatory uncertainty, thus reducing the risk premium new entrants may require. The Settlement Agreement allows parties to challenge key inputs into the auction prior to the running of the auction. Not later than 90 calendar days prior to each

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[29] *See* Settlement Agreement at section 4.C and *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332, 344-45 (1956) (*Mobile*) and *FPC v. Sierra Pacific Power Co.*, 350 U.S. 348, 355 (1956) (*Sierra*).

FCA, ISO-NE will make an informational filing with the Commission in which it will identify: 1) the capacity zones applicable to that auction; 2) the resources qualified to participate in the FCA or reconfiguration auction specifically; and 3) conclusions of the Market Monitor regarding the acceptability of bids. Interested parties will have 15 days to file comments on or challenges to the determinations in that informational filing. Unless the Commission issues an order to the contrary within 75 calendar days following the informational filing, ISO-NE will use the determinations in the informational filing in the next FCA.

37. Results from FCAs will be filed with the Commission by ISO-NE pursuant to section 205 of the FPA. Parties will have 45 days to file objections to the auction results, and this will be the only means of challenging such results. Once this process is complete, the prices will be subject to the *Mobile-Sierra* public interest standard under section 4.C of the Settlement Agreement. Section 5 of the Settlement Agreement provides that ISO-NE's internal market monitoring unit will issue a full report analyzing the operations and effectiveness of the FCM 180 days after the second FCA and annually in its markets report thereafter.

III. Procedural Matters

38. Comments on the Settlement Agreement were filed by the following parties: Berkshire Power Company, LLC (Berkshire), Consolidated Edison Energy, Inc. (ConEd), EnerNOC, Inc. (EnerNOC), Exelon Generation Company, LLC and Exelon New England Holdings (Exelon), Industrial Energy Consumer Group (IECG), Load Supporters,[30] Long Island Power Authority and

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[30] Load Supporters are: Connecticut Department of Public Utility Control, Connecticut Office of Consumer Counsel, New Hampshire

LIPA (LIPA), Maine Parties,[31] Objecting Parties,[32] PPL EnergyPlus, LLC and PPL Wallingford Energy LLC (PPL), PSEG Energy Resources & Trade LLC (PSEG), Reading Municipal Light Department (Reading), and Select Energy, Inc. (Select). NSTAR Electric and Gas Corporation (NSTAR) filed supplemental comments in opposition to the Settlement Agreement.

39. Reply comments were filed by the following parties: American National Power, Inc., Granite Ridge Energy, LLC and TransCanada Power Marketing Ltd. (American National Power), Calpine Energy Services, L.P. and Calpine Eastern Corporation (Calpine), Capacity Suppliers,[33] Connecticut Municipal Electric Energy Cooperative (CMEEC), ISO-NE, Lake Road Generating Company, L.P. (Lake Road), Load Supporters, Maine Parties, Massachusetts Municipal Wholesale Electric Company and

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Public Utilities Commission, Rhode Island Public Utilities Commission, Rhode Island Division of Public Utilities and Carriers, Vermont Public Service Board, Vermont Department of Public Service, and The Connecticut Power and Light Company, by its agent Northeast Utilities Service Company.

[31] Maine Parties are Maine Public Utilities Commission and Maine Public Advocate.

[32] Objecting Parties are: Attorney General of the Commonwealth of Massachusetts, Richard Blumenthal, Attorney General for the State of Connecticut, NSTAR Electric and Gas Corporation, NEPOOL Industrial Customer Coalition, and The Energy Consortium (which includes President and Fellows of Harvard College, Brandeis University, Polaroid Corporation, USG Corporation, and Massachusetts Institute of Technology).

[33] Capacity Suppliers are: Boston Generating, LLC, Mystic Development, LLC, Mystic I, LLC, Fore River Development, LLC (collectively, "Boston Gen"), FPL Energy, LLC, Mirant Americas Energy Marketing, LP, Mirant Kendall, LLC, Mirant Canal, LLC, Entergy Nuclear Generation Company, LLC, Entergy Nuclear Vermont Yankee, LLC, Dominion Resources, Inc., Dominion Nuclear Connecticut, Inc. and Dominion Energy Marketing, Inc.

Reading (MMWEC), Milford Power Company, LLC (Milford), National Grid USA (National Grid), New England Power Pool Participants Committee (NEPOOL), New York Independent System Operator, Inc. (NYISO), NRG Companies (NRG),[34] Objecting Parties, and PPL. On April 11, 2006, Exelon filed a motion for leave to file reply comments out of time and reply comments. On June 6, 2006, Black Oak Energy, LLC (Black Oak) and EPIC Merchant Energy, LP (EPIC) filed a motion to intervene out of time and a motion to file limited comments out of time.

40. We will accept Exelon's motion to file reply comments out of time. We deny, however, the motion of Black Oak and EPIC to intervene and file initial comments at this late stage of the proceeding. We find that granting Black Oak and EPIC's motion would be disruptive given that its motion was filed less than a month before the June 30, 2006 date by which the Commission must act on the Settlement Agreement. Moreover, since the comments amount to a protest to the Settlement Agreement, granting the motion would prejudice those supporting the settlement by effectively denying them the opportunity to reply under the Commission's rules. Black Oak's and EPIC's arguments that they were not aware of the Settlement Agreement's impact on their interests are unpersuasive; the Settlement Agreement was filed three months before Black Oak and Epic sought to intervene, and was considered in the New England Power Pool stakeholder process, which should have alerted active participants in the New England markets like Black Oak and EPIC that their interests might be impacted.

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[34] NRG includes Devon Power LLC, Montville Power, Connecticut Jet Power and Middletown Power.

IV. Discussion

A. General Comments in Support of the Settlement

41. The following parties filed comments in support of the Settlement Agreement: Load Supporters, Reading, EnerNOC, ConEd, Berkshire, Exelon, Select, and Lake Road. In general, these parties support acceptance of the Settlement Agreement without modification. For the most part, those submitting general comments supporting the settlement emphasize that it is the product of a complex and difficult negotiation and represents a careful and interconnected balancing of interests. Accordingly, most state that modifying any portion of the Settlement Agreement could upset this balance and risk unraveling the settlement entirely.

42. ConEd states that the settlement corrects deficiencies in the current market and is the most likely construct to attract and retain the resources needed for reliability. Exelon supports the request that the settlement be approved in its entirety as just and reasonable and in the public interest. Exelon further states that the forward commitment provision will allow existing generators to make informed decisions and will benefit load by facilitating a robust and cost effective regional planning process. Select asserts that the FCM accommodates various load parties by basing the compensation mechanism on a market outcome.

43. Load Supporters state that the FCM is designed to produce just and reasonable results and is a substantial benefit to New England electricity customers compared with LICAP. Load Supporters state that the FCM contains many of the elements derived from prior alternatives, including the New England Resource Adequacy

Market[35] and the New England Locational Resource Adequacy Market,[36] as well as the Central Resource Adequacy Market,[37] and rests on facts developed in the evidentiary record. Load Supporters state that the settlement resolves several of the material flaws that the parties had with the LICAP proposal by requiring load to purchase only the amount of capacity needed, by facilitating new entrant participation (including demand-side resources) through a three-year forward commitment period, and by using an auction to produce the lowest reasonable cost of new entry. Load Supporters also state that that another important feature of the settlement is that it allows load the opportunity to self-supply or contract bilaterally; thereby providing a hedge against volatility—an important feature for Connecticut, New Hampshire, and Vermont. Load Supporters also state that the Settlement Agreement provides a stakeholder process that includes participation by the New England state regulatory agencies, to determine the installed capacity requirement.

44. More specifically, Load Supporters state that the FCM increases the elasticity of supply, *i.e.*, an upward sloping supply curve, by procuring capacity three years in advance with a minimum one-year commitment period,

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[35] *See* "Statement in Support of the New England Resource Adequacy Market," filed by Massachusetts Department of Telecommunications and Energy *et al.* in Docket No. ER03-563-030 (Sept. 13, 2005).

[36] *See* "Four State Commissions' Proposed Alternative to LICAP", filed by Rhode Island Public Utilities Commission, New Hampshire Public Utilities Commission, Vermont Public Service Board, Vermont Department of Public Service and Maine Public Utilities Commission in Docket No. ER03-563-030 (Sept. 13, 2005) (describing the proposed New England Locational Resource Adequacy Market).

[37] *See* ISO-NE March 1, 2004 compliance filing in Docket ER03-563-030 at 52.

by enabling potential new entrants to compete with existing suppliers, and by clearly defining the obligations of capacity suppliers. According to Load Supporters, this planning period enables existing capacity to provide quantities responsive to price, provides relief from reliability-based barriers to exit and enables demand-side resources to respond to price as well. They compare this feature to LICAP, which would commit resources only one month in advance of their obligation to perform and commit them for only one month at a time.

45. Load Supporters also state that the FCM procures only the amount of capacity necessary to maintain reliability, compared to LICAP which set a target of 5.4 percent above the installed capacity requirement and would pay suppliers for surpluses up to 15 percent above the installed capacity requirement. Load Supporters stated that this permits capacity in excess of the amount needed to retire, mothball, or sell into other markets. Load Supporters state that, unlike the LICAP's proposed administratively determined demand curve, the FCM sets price through a competitive auction. Load Supporters state that the FCM includes multiple constraints on market power. Load Supporters also state that the ISO-NE Market Monitoring Unit will evaluate the performance of the FCM and will prepare annual reports on the operation of the market.

46. In addition, Load Supporters state that, unlike LICAP, the FCM expressly defines the commitments that supply must make in return for load's substantial capacity payments. Load Supporters also state that the minimum year-long commitment period for capacity resources locks in price and firm obligations giving load certainty over price and reliability while giving suppliers certainty over revenue. They also note that the FCM further reduces risks for new capacity investment by

providing 1) an option for new suppliers to lock in a five-year commitment period, 2) annual reconfiguration auctions to cover the risk of non-performance, and 3) a flexible financial assurance policy.

47. Load Supporters argue that the proposal to adjust the monthly capacity payments determined by the FCA not only reduces incentives for suppliers to withhold in the energy market but also provides a hedge for load against energy market price spikes. Load Supporters state that the Shortage Event mechanism will reward resources that perform during periods of system stress and penalize those resources that fail to perform. Load Supporters also state that availability will be improved with the settlement provisions regarding gas delivery.

48. Lake Road states that the settlement should be approved as in the public interest. Lake Road asserts that in the long-term, the FCM will provide a more sophisticated method to encourage the right amount of capacity in the right locations. NEPOOL supports the settlement and, without taking positions on the issues, opposes any change or condition that would upset the negotiated balance of the Settlement Agreement.

B. General Comments in Opposition to the Settlement

49. Comments in opposition to the Settlement Agreement are addressed in detail below.

C. Standard of Review and Commission Conclusions Regarding Overall Justness and Reasonableness of the Settlement

50. In the explanatory statement, Settling Parties note that the Commission "'can approve contested settlements as long as it determines that the proposal will establish

just and reasonable rates.'"[38] They state that the Commission must support its decision to accept a contested settlement with substantial evidence or a finding that there is no genuine issue of material fact as to the contested matter. Noting the four approaches in *Trailblazer*[39] that the Commission may utilize to address a contested settlement, Settling Parties urge the Commission to approve the Settlement Agreement as a package under the second *Trailblazer* approach, which (as discussed below) allows the Commission to approve a settlement as a package if it determines that the overall result of the settlement is just and reasonable.[40] Settling Parties argue that the Settlement Agreement is a complete package that reflects a complex compromise among the affected parties, and that while those parties may oppose some individual components within the agreement, they have agreed to the settlement as a package. Settling Parties contend that changing any aspect of the Settlement Agreement would upset the balance achieved among the parties and result in calls to change

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[38] Explanatory Statement at 4, *citing New Orleans Public Service, Inc. v. FERC*, 659 F.2d 509, 512 (5th Cir. 1981) (*citing Placid Oil Co. v. FPC*, 483 F.2d 880, 893 (5th Cir. 1973), *aff'd sub nom. Mobil Oil Corp. v. FPC*, 417 U.S. 283, 312-13 (1973)).

[39] *Trailblazer Pipeline Company*, 85 FERC ¶ 61,345 (1998), *order on reh'g*, 87 FERC ¶ 61,110 (1999) (*Trailblazer*). The four approaches laid out in *Trailblazer* are: (1) Commission renders a binding merits decision on each contested issue, (2) Commission approves the settlement based on a finding that the overall settlement as a package is just and reasonable, (3) Commission determines that the benefits of the settlement outweigh the nature of the objections, and the interests of the contesting party are too attenuated, and (4) Commission approves the settlement as uncontested for the consenting parties, and severs the contesting parties to allow them to litigate the issues raised.

[40] In their comments, Exelon and Select, among other commenters, support this request.

other aspects of the agreement. Settling Parties also assert that severing contesting parties (under the fourth *Trailblazer* approach) is inappropriate here because the settlement creates a structure applicable to all generation and load in New England, meaning that objecting parties cannot continue to litigate the transition charges or market design without affecting the rates charged to and received by other parties and upsetting the balance achieved in the Settlement Agreement.

51. Parties submitting comments on the Settlement Agreement also discussed the applicable standard of review. IECG, Objecting Parties, Load Supporters and American National Power all state that to approve a contested settlement, the Commission "must make 'an independent finding supported by substantial evidence on the record as a whole' that the Settlement is just and reasonable[,] . . . produce[s] a reasonable resolution of the proceedings" or that "'there is no genuine issue of material fact.'"[41] Additionally, IECG states that the fact that a settlement agreement was agreed to by many parties does not guarantee that the result is just and reasonable.[42] Similarly, Objecting Parties argue that the number of parties supporting a proposed settlement, while a factor to consider, is not dispositive in determining whether to approve the settlement.[43] American National

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[41] *See, e.g.*, Comments in Opposition to the Proposed Settlement Agreement of IECG at 2, *citing Mobil Oil Corp. v. FPC*, 417 U.S. 283, 314 (1974) and *San Diego Gas & Electric Company*, 108 FERC ¶ 61,002 at 61,010-011 (2004).

[42] Comments in Opposition to the Proposed Settlement Agreement of IECG at 3-4, *citing NorAm Gas Transmission Co. v. FERC*, 148 F.3d 1158 (D.C. Cir. 1998).

[43] *See* Comments in Opposition to Settlement of Objecting Parties at 12-13, *citing NorAm Gas Transmission Co. v. FERC*, 148 F. 3d 1158 (D.C. Cir. 1998) and *Laclede Gas Co. v. FERC*, 997 F.2d 936 (D.C. Cir. 1993).

Power adds that the Commission has broad discretion when considering contested settlements.[44]

52. Maine Parties, Load Supporters and American National Power all discuss the *Trailblazer* approaches to addressing contested settlements, particularly the second approach. Load Supporters note that the Commission explained the second *Trailblazer* approach in the context of the approval of contested settlements in *Indicated Shippers*[45] and *Pacific Gas Transmission Co.*[46] In those cases, the Commission emphasized that to be approved as a package, the settlement rates must be shown to be less than or equal to the just and reasonable rates that would likely result from litigation.[47] Load Supporters also note that in *Trailblazer*, the Commission stated that when parties ask that a settlement be considered as a package, it would "'try to honor the parties' intent' and consider the justness and reasonableness of the package in its entirety."[48] ISO-NE, in reply to comments opposing the Settlement Agreement, adds that the Commission has previously held that it may approve a contested settlement as a package if the overall result is just and reasonable even if some aspects of the settlement are problematic.[49] Further, ISO-NE notes that a contested

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[44] Reply Comments of American National Power at 7, *citing Arctic Slope Regional Corp. v. FERC*, 832 F.2d 158, 164 (D.C. Cir. 1987).

[45] *Indicated Shippers v. Sea Robin Pipeline Co.*, 81 FERC ¶ 61,146 (1997) (*Indicated Shippers*).

[46] 82 FERC ¶ 61,289 (1998).

[47] Initial Comments of Load Supporters in Support of Offer of Settlement at 9-10, *citing Trailblazer*, 85 FERC ¶ 61,345 at 62,342-343.

[48] Initial Comments of Load Supporters in Support of Offer of Settlement at 10.

[49] Reply Comments of ISO NE at 16, *citing San Diego Gas & Electric Co. v. Sellers of Energy Ancillary Services*, 108 FERC ¶ 61,002 at 61,011 (2004).

settlement may be approved if, as a whole (considering both contested and uncontested issues), it provides a just and reasonable result.[50] Finally, it states that "[t]he Commission need only find that the overall package, resulting from the give and take of the bargaining which led to the settlement, falls within" the just and reasonable range.[51]

53. IECG asserts that the Settlement Agreement does not provide a just, reasonable or otherwise lawful resolution of the proceeding, and that the Settling Parties have not offered substantial record evidence that the agreement will result in just and reasonable rates or that the settlement will provide contesting parties with a result that is at least as good as the result they could achieve through litigation on the merits. According to IECG, the Settling Parties have only provided a comparison between the rates the Commission might have approved when ruling on the Initial Decision and the transition payments, which it argues is insufficient to support the increased costs contemplated by the transition period or to allow the Commission to conclude that parties opposing the agreement would not be better off through continued litigation.[52]

54. Maine Parties, focusing on the procedural avenues in *Trailblazer*, argue that the Commission's only options are to conditionally accept the settlement, sever the contested issues and initiate further proceedings to resolve

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[50] Reply Comments of ISO-NE at 16, *citing Trailblazer*, 85 FERC ¶ 61,345 at 62,342.

[51] *Id.*, *citing Trailblazer*, 85 FERC ¶ 61,345 at 62,343.

[52] As discussed further below, IECG notes that the LICAP mechanism recommended in the Initial Decision would have included elimination of RMR agreements, improved availability metrics, and included other features that make a comparison to the transition payments insufficient.

those issues, or reject the entire settlement and initiate hearing procedures. Like IECG, they contend that the record lacks the substantial evidence necessary to resolve the contested material issues of fact on the merits, approve the overall settlement as a package, or find that the benefits of the settlement outweigh the objections. Maine Parties also argue that the transition payments cannot be found just and on reasonable based on a comparison to the rates that might have resulted from the Initial Decision, contrary to the arguments of Load Supporters. According to Maine Parties, neither *Trailblazer* nor the precedents it cites suggest that the Initial Decision, which was never reviewed by the Commission and later set aside, should be considered the likely outcome of litigation. Additionally, Maine Parties note that in *Indicated Shippers* (cited by Load Supporters), the Commission, after finding that the parties had raised genuine issues of material fact, went on to determine the issues on the merits after the parties agreed that the record contained substantial evidence upon which the Commission could make a merits determination. Maine Parties also note that in *Indicated Shippers* the Commission engaged in a thorough analysis to determine the likely outcome of litigation, which Load Supporters do not suggest the Commission undertake here.

55. Responding to arguments that the record lacks the substantial evidence necessary to approve the Settlement Agreement, ISO-NE argues that the Affidavits submitted with the Agreement, the written proposals for alternatives to LICAP submitted prior to the oral argument, and the oral argument itself all represent substantial evidence upon which to base approval of the settlement. Moreover, ISO-NE states that the extensive record developed in the LICAP proceeding and the Commission's orders in other proceedings concerning the development

of capacity markets provide substantial evidence.[53] ISO-NE also states that the Commission has previously held that it is not limited to opinion testimony and may rely on a wide range of materials as substantial evidence, including its own orders, tariffs and certificates on file, and its general policies.[54]

56. Load Supporters, as well as ISO-NE and Capacity Suppliers, also contend that the parties objecting to the settlement have raised no genuine issues of material fact.[55] ISO-NE argues that factual contentions made by opponents of the Settlement Agreement are either not valid and thus do not rise to the level of material facts, or are questions of law and policy and not facts themselves.

57. In reply comments, ISO-NE argues that the Commission has broad discretion to make policy determinations on technical matters of market and rate design, and that it has the authority to decide, based on its expertise, that the Settlement Agreement is just and reasonable as a package.[56] Additionally, in response to arguments from opponents of the Settlement Agreement regarding the weight to be given to the amount of support for the agreement, ISO-NE argues that the Commission's prece-

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[53] ISO-NE notes that the FCM incorporates features of many other models that the Commission has received evidence on in this and other proceedings. *See* Reply Comments of ISO-NE at 18-19.

[54] *Id.* at 18, *citing Williston Basin Interstate Pipeline Co.*, 68 FERC ¶ 61,357 at 62,432-33 (1994).

[55] According to ISO-NE, "it is well settled that 'a genuine issue of material fact sufficient to preclude approval of a settlement agreement must be a dispute of the basic facts underlying the settlement.'" Reply Comments of ISO-NE at 12 (citation omitted).

[56] Reply Comments of ISO-NE at 10-11, *citing in part Elec. Consumers Res. Council v. FERC*, 407 F.3d 1232 (D.C. Cir. 2005); *Fuels Research Council, Inc. v. FPC*, 374 F.2d 842 (7th Cir. 1967); *Entergy Servs. v. FERC*, 319 F.3d 536 (D.C. Cir. 2003).

dent strongly favors settlements, particularly those that have broad support, and that the Commission may approve a settlement even when a particular aspect of it deviates from Commission policy.[57]

Commission Conclusion

58. The Commission has broad authority and discretion under Rule 602(h) of its regulations to address contested settlements.[58] Courts have confirmed the Commission's authority to approve contested settlements, so long as the proposal will establish just and reasonable rates.[59] Under Rule 602(h), the Commission may decide the merits of the contested issues if the record contains substantial evidence on which to base a reasoned decision or if the Commission determines that there is no genuine issue of material fact. If the Commission finds that the record lacks substantial evidence or that the contesting parties or issues cannot be severed, the Commission may establish hearing procedures to supplement the record, or it may take other appropriate action.[60]

59. In *Trailblazer*, the Commission explained at length the standards and procedures it employs in ruling on contested settlements. The Commission stated that, in re-

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[57] Reply Comments of ISO-NE at 20 (citations omitted). ISO-NE also says that this agreement does not deviate from any applicable Commission policy.

[58] 18 C.F.R. § 385.602(h) (2005).

[59] *See New Orleans Public Service, Inc. v. FERC*, 659 F.2d 509, 511-12 (5th Cir. 1981), *citing Placid Oil Co. v. FPC*, 483 F.2d 880, 893 (5th Cir. 1973), *aff'd sub nom. Mobil Oil Corp. v. FPC*, 417 U.S. 283, 312-13 (1974).

[60] *See* 18 C.F.R. § 385.602(h)(1)(ii)(B) (2005). In *Arctic Slope Regional Corp. v. FERC*, 832 F.2d 158, 164 (D.C. Cir. 1987), the court observed that "the breadth of discretion trumpeted by Rule 602(h)(1)(ii)(B) is manifest."

viewing a settlement, it must first determine whether the settlement presents an acceptable outcome for the case that is consistent with the public interest. The Commission acknowledged the value of settlements, but stated that some cases may involve an overriding public interest that outweighs the interest in achieving a settlement. In such instances, the Commission has modified those settlements to be consistent with Commission policy.[61]

60. If the Commission concludes that a contested settlement provides an acceptable outcome for a case, it must next determine the approach it will employ to address the contested issues. In *Trailblazer*, the Commission explained four approaches it has taken for approving a contested settlement despite the objections of the contesting party. Under the first approach, if there is an adequate record, the Commission can address each of the contested issues on the merits, approving the settlement if the Commission finds that each of the contesting party's contentions lacks merit. This approach is appropriate where the issues are primarily policy issues or the parties have agreed that the record is sufficient to decide the issues on the merits. However, the Commission explained that, even where the settlement cannot be approved under the first approach, it may be approved under other approaches. Thus, under the second approach, even if some individual aspects of a settlement may not be just and reasonable standing alone, the Commission may approve a contested settlement as a package if the overall result of the settlement is just and reasonable. Under this approach, the Commission will not make a merits decision on whether each element of the settlement package is just and reasonable but will determine whether the overall package falls within a zone of reasonableness.[62]

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[61] *Trailblazer*, 85 FERC at 62,341.

[62] *Id.* at 62,342; *order on reh'g*, 87 FERC at 61,440.

When the Commission takes this approach, it need not find that the settlement rate is exactly the rate the Commission would find just and reasonable on the merits after litigation and need only find that the settlement rate falls within a zone of reasonableness. The Commission must also find under this approach that the contesting party would be in no worse position under the settlement than if the case were litigated.

61. Under the third approach, if the settlement is not found to satisfy the just and reasonable standard, the Commission may approve the settlement where the benefits of the settlement outweigh the nature of the objections, and the contesting parties' interest is too attenuated so that the settlement may be approved under the fair and equitable standard applicable to uncontested settlements. The third alternative usually has included a finding that the contesting party would have another forum in which to raise its contentions. The fourth approach is severance of the contesting party, permitting that party to obtain a litigated result, and approving the settlement as to the consenting parties.

The Outcome Under the Settlement Agreement Meets the *Trailblazer* Standards for Approval

62. Pursuant to our *Trailblazer* standards, the Commission first finds that the Settlement Agreement is consistent with the public interest.[63] The results, including the long-term FCM and short-term transition mechanisms, resolve the deficiencies in New England's existing capacity market identified by the Commission and the parties to this case. As noted above, the Commission instituted

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[63] *See NAACP v. FPC*, 425 U.S. 662, 670 (1976) (noting that the use of the words "public interest" in the FPA is a "charge to promote the orderly production of plentiful supplies of electric energy and natural gas at just and reasonable rates.")

these section 206 proceedings in the April 25 Order in response to the compensation problems faced by generating resources that are needed for reliability but could not obtain sufficient revenues in the markets to continue operation. The Commission stated that its long-term goal was to approve a locational or deliverability mechanism to ensure that capacity resources in New England are appropriately compensated, particularly in highly constrained areas.[64] In the June 2 Order establishing hearing procedures on ISO-NE's proposed LICAP mechanism, the Commission again found that New England faced significant Reliability Compensation Issues in both the short and long terms, particularly in constrained areas.[65] In analyzing the proposed LICAP mechanism, the Commission noted that a capacity market mechanism should both provide adequate revenues to appropriately compensate (and keep in service where needed for reliability) existing capacity resources and provide incentive for the development of new infrastructure in areas where it is most needed.[66]

63. Moreover, as the record in this proceeding has developed, both the parties to this case and the Commission have recognized the necessity of a workable capacity market to meet the need for additional infrastructure in New England. While the region has sufficient capacity to meet reliability requirements today, reserve margins are barely adequate, and deficits are predicted in the very near future.[67] At the oral argument, the parties almost

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[64] April 25 Order at P 37.

[65] June 2 Order at P 35 *et seq.*, *citing PMJ Interconnection, L.L.C.*, 107 FERC ¶ 61,112 (2004).

[66] *See* June 2 Order at P 40-43, 49-52; *see also* November 8 Order on Rehearing at P 65-67.

[67] *See, e.g.*, Executive Summary of the ISO-NE Regional System Plan 2005, attached to Notice of Proposed Speakers and Time

unanimously agreed that the status quo presents significant problems that the Commission must address.[68] The record from the oral argument is replete with virtually unchallenged statements that existing generators needed for reliability are not earning sufficient revenues (and are in fact losing money), and that additional infrastructure is needed soon to avoid violations of reliability criteria.[69]

64. The Settlement Agreement provides necessary solutions to resolve these deficiencies in New England's current ICAP market and the resulting impacts those deficiencies have had on New England's infrastructure, and is well supported both by the record and by Commission policy.[70] The Settlement Agreement incorporates the primary components of the two alternatives proposed by state entities and discussed at oral argument: a forward resource auction, a descending clock auction, penalties for non-performance, and a phase-in or transition period.[71]

Allocation for Oral Argument filed by ISO-NE in Docket No. ER03-563-030 (Sept. 14, 2005).

[68] Tr. of Oral Argument at 252:8-12 (Chairman Kelliher noting that "every presenter, other than one, agreed that the Commission has to take some kind of action").

[69] *See, e.g.*, Tr. Of Oral Argument at 36:21-24; 44:7-11; 76:6-22; 150:9-151:6; 167:1-4; 237:9-12.

[70] *See, e.g., PJM Interconnection, L.L.C.*, 107 FERC ¶ 61,112 at 15 (noting that the Commission, in addressing Reliability Compensation Issues, will take account of both present circumstances and expected needs).

[71] *See, e.g.*, Tr. of Oral Argument at 148 *et seq.* and 165 *et seq.*; *see also* "Statement in Support of the New England Resource Adequacy Market," filed by Massachusetts Department of Telecommunications and Energy, Connecticut Department of Public Utility Control *et al.* in Docket No. ER03-563-030 (Sept. 13, 2005); "Four State Commissions' Proposed Alternative to LICAP", filed by Rhode Island Public Utilities Commission, New Hampshire Public Utilities Commission,

65. First, both the FCM and the interim transition mechanism will provide the revenues needed by generators to keep them in operation to preserve reliability.[72] Below, we discuss in more detail the justness and reasonableness of the transition payments as a short-term measure to ensure that existing generating units remain available. The FCM construct, when fully implemented, will provide a market-based mechanism to appropriately value capacity resources based on their location, satisfying cost-causation principles.[73] Many of the load representatives were particularly concerned that the LICAP proposal did not "impose any reciprocal obligation on these generators to continue operating over the long-term."[74] The FCM addresses these concerns by requiring new capacity that bids in the FCAs to meet milestones regarding project feasibility and an interconnection analysis showing the impact of connecting to the transmission grid. In addition, the forward-looking nature of the FCM will provide appropriate signals to investors when new infrastructure resources are necessary with sufficient lead time to allow that infrastructure to be put into place before reliability is sacrificed.[75] The locational component

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Vermont Public Service Board, Vermont Department of Public Service and Maine Public Utilities Commission in Docket No. ER03-563-030 (Sept. 13, 2005) (describing the proposed New England Locational Resource Adequacy Market).

[72] *See, e.g.*, Brief Opposing Exceptions of ISO-NE at 2-3; *ISO-NE 2004 Annual Markets Report at* 111-12, *available at* http://www.iso-ne.com/markets/mkt_anlys_rpts/annl_mkt_rpts/2004/2004_annual_markets_report_.pdf.

[73] *See, e.g., PJM Interconnection, L.L.C.*, 107 FERC ¶ 61,112 at 19-20; *PJM Interconnection, L.L.C.*, 115 FERC ¶ 61,079 at P 49-51 (2006).

[74] Brief on Exceptions of the New England Conference of Public Utility Commissioners at 2.

[75] *See PJM Interconnection, L.L.C.*, 115 FERC ¶ 61,079 at P 67-72.

of the FCM will ensure that the addition of new infrastructure is targeted to where reliability problems are most imminent.[76]

66. The fact that this Settlement Agreement resolves all of the outstanding issues in a difficult, contentious and lengthy matter also weighs in our decision that the settlement is consistent with the public interest. The Settlement Agreement represents difficult compromises among the diverse parties to this proceeding that, if found just and reasonable, should be honored. From October 2005 until March 2006, over 175 representatives, including representatives from all of the state public utility regulatory agencies, as well as representatives of transmission owners, generators, power traders and marketers, demand response and intermittent resource owners, consumer-owned utility systems and end users, engaged in informal and formal settlement negotiations.[77] Moreover, the Settlement Agreement, by ending this protracted litigation, will bring a needed measure of stability and allow New England to move forward on other market enhancements. Additionally, the Commission strongly favors settlements, particularly in difficult cases like the instant proceeding.[78]

67. The Settlement Agreement is also consistent with the public interest because it comports with the recently expressed intent of Congress regarding this case. In section 1236 of the Energy Policy Act of 2005, Congress noted the concerns voiced by the governors of the New England states regarding the LICAP mechanism, and

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[76] *Id.* at P 49-51.

[77] Reply Comments of NEPOOL Participants Committee at 2.

[78] *See, e.g., Idaho Power Co.*, 109 FERC ¶ 61,308 at P 5 (2004) (stating that the Commission is "strongly in favor of settlements, particularly in cases [that are] hotly contested and complex.").

declared that the Commission should carefully consider their objections.[79] The oral argument held in this proceeding considered the states' objections to the LICAP mechanism and their proposals for alternative capacity market designs. Settlement discussions followed regarding alternatives. This settlement is a product of those discussions, and includes measures to address many of the objections voiced by the states, responding to the sense of Congress in section 1236.

The Overall Result of the Settlement Agreement is Just and Reasonable

68. To address the contested issues raised by those opposing the Settlement Agreement, we will use the second approach articulated in *Trailblazer*, as requested by the Settling Parties.[80] Using this approach here is appropriate for several reasons. First, we find that the record in this proceeding is sufficient to allow us to make a determination that as a package, the settlement is just and reasonable. The record includes, among other items, both written submissions and oral argument testimony concerning various approaches to designing New England's capacity market, data regarding current and projected capacity prices in New England, price projections under both the settlement and various LICAP demand curve proposals, and information regarding the current and projected need to develop new infrastructure in New England. Moreover, with regard to the transition payments (the most heavily protested aspect of the Settlement Agreement), we agree with the presiding Settle-

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[79] Energy Policy Act of 2005, Pub. L. No. 109-58, § 1236, 119 Stat. 961 (2005).

[80] *See Trailblazer*, 87 FERC at 61,440 (stating that the Commission will try to honor the parties' intent that a settlement be considered as a package).

ment Judge that this record provides a thorough basis for the Commission's decision to approve the Settlement Agreement as a package.[81]

69. In addition to honoring the intent of the Settling Parties, the second of the four *Trailblazer* approaches is the most appropriate here. It would be inappropriate to strictly apply the first approach here because the Settlement Agreement contains several complex and interrelated features intended to be considered as an overall package, and altering any of those features will have consequences for other portions of the settlement. We will consider the contested issues below, however, to ensure the overall justness and reasonableness of the settlement as a package. The third approach is unavailable here because while we believe that the settlement, as a package, provides significant benefits that outweigh the nature of the objections raised, the parties raising such objections (which include load representatives of certain states) have more than an attenuated interest. Finally, the fourth approach is not appropriate here because the Settlement Agreement provides a capacity market structure that will apply throughout New England, making it impossible to effectively sever any of the contesting parties to allow them to further pursue the issues they raise, since the resolution of those issues will affect all the parties.

70. Applying the second *Trailblazer* approach here, we find that the parties objecting to the Settlement Agreement would "be in no worse position under the terms of the settlement than if the case were litigated," and that the Settlement Agreement, as a package, achieves an

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[81] *Report on Contested Settlement by Settlement Judge, Devon Power LLC*, 115 FERC ¶ 63,013 (2006).

overall just and reasonable result within a zone of reasonableness.[82]

71. We find that the Settlement Agreement achieves an overall just and reasonable result for many of the same reasons we articulated above in finding that it provided an acceptable outcome for this case consistent with the public interest. The settlement package, including both the FCM and the interim transition mechanism, resolves the issues raised in this proceeding concerning the under-compensation of capacity resources in New England, and provides the appropriate market structure to ensure that generating resources are appropriately compensated based on their location and contribution to system reliability and provides incentives to attract new infrastructure where needed. As discussed below, the key price-determining parameters of the FCM descending clock auction (such as CONE) are appropriate and adequately supported in the record. "A just and reasonable rate is not a product of any single formula, but is instead a rate within a broad ambit of various rates which may be just and reasonable," and as we discuss below, none of the parties opposing the Settlement Agreement has shown that the settlement (or any specific aspect of it) is outside of this "range of reasonableness."[83]

72. We find that the parties opposing the Settlement Agreement would be no worse off under the settlement than through continued litigation. The affidavits and other evidence provided by the Settling Parties and others in support of the Settlement Agreement show that

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[82] *Trailblazer*, 87 FERC ¶ 61,110 at 61,339.

[83] *See Belco Petroleum Corp. v. FERC*, 589 F.2d 680, 689 (D.C. Cir. 1979), *citing Permian Basin Area Rate Cases*, 390 U.S. 747, 767 (1968); *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 602 (1944); *FPC v. Natural Gas Pipeline Co.*, 315 U.S. 575, 585-86, (1942).

the settlement, and particularly the transition period, results in rates for capacity that are lower than the projected payments under ISO-NE's proposed demand curve (which we note was adopted in the Initial Decision) and that are comparable to the rates under alternative demand curves proposed at the hearing, bringing those rates within a range that we find is just and reasonable.[84] We address this issue more specifically below with regard to the opposing parties' specific arguments that the transition payments cannot be approved on the basis of a comparison with the rates that would have resulted under LICAP.[85]

73. Further, we note that, while Objecting Parties' are correct that the level of support for the Settlement Agreement is not dispositive, the Commission can give weight to the broad-based support the Settlement Agreement received.[86] In this difficult, contentious proceeding, the Settlement Agreement was either supported or not opposed by 107 of the 115 parties in the proceeding.[87] We agree with the Settlement Judge's characterization of

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[84] *See, e.g.*, Explanatory Statement in Support of Settlement Agreement at 34-40; Attachment 6 to Settlement Agreement (Affidavit of David LaPlante); Comments of Load Supporters and Affidavit of Miles O. Bidwell, Jr., Ph.D.

[85] For example, we address below Maine Parties' contentions that the Commission should consider a lower LICAP demand curve for Maine when comparing the transition payments to the LICAP mechanism, among other issues.

[86] *See Laclede Gas Co. v. FERC*, 997 F.2d 936, 946 (D.C. Cir. 1993); *NorAm Gas Transmission Co. v. FERC*, 148 F.3d 1158, 1164-65 (D.C. Cir. 1998).

[87] *See Report on Contested Settlement by Settlement Judge, Devon Power LLC*, 115 FERC ¶ 63,013 at P 15 (2006).

this level of support as "quite extraordinary and . . . noteworthy."[88]

D. Specific Issues Raised in Comments on Proposed Settlement Agreement and Reply Comments, and Commission Conclusions

74. As noted above, while we are approving the Settlement Agreement as just and reasonable as a package under the second approach of *Trailblazer*, we analyze below the specific issues raised by parties opposing the settlement to ensure that each, when considered as part of the overall package, meets the standards articulated in *Trailblazer*.

1. Transition Mechanism

75. As noted above, during the transition period, fixed payments will be paid to all installed capacity. These payments are intended to serve as a bridge to the FCM, and are not locational. All suppliers will receive transition payments, though these payments will be netted against RMR payments as well as adjusted to account for outages.

76. Several parties—IECG, Maine Parties and Objecting Parties—oppose the transition payments for a variety of reasons. First, they argue that there is no evidence to support the level of the transition payments. Objecting Parties assert that there is no record evidence that examined the amount of revenue required to keep existing resources available and nothing to indicate that the transition payments were compared against such a study. Maine Parties assert that there is insufficient evidence in the record on which the Commission may base a just and reasonable finding and that "a hearing would reveal that the transition payments are unjust and unreasonable" as

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[88] *Id.*

they exceed "what is needed by generators" to supplement revenues from other markets.[89] IECG asserts that Settling Parties do not make a case that the costs of the transition payments are equivalent to the costs of the transition period. Maine Parties submit that the rationale that lower rates are necessarily just and reasonable is inconsistent with Commission precedent.[90] Maine Parties also state that ISO-NE has failed to justify that transition payments are necessary to retain existing generation in Maine. Maine Parties submit further that most Maine suppliers would continue to operate without transition payments as they have been setting energy prices.

77. IECG, Maine Parties and Objecting Parties further argue that the transition payments are not connected to an added service or benefit. The parties note that during the transition period, some suppliers will be paid in the locational forward reserves market and some will continue to be paid under RMR contracts. Objecting Parties assert that, rather than target financially distressed generation needed for reliability, the transition payments simply extend capacity payments to all capacity suppliers. Objecting Parties state that the transition payments are "money for nothing"[91] and argue that existing RMR contracts should be eliminated at the beginning of the transition period. IECG similarly notes that there is no restraint upon RMR agreements. IECG states that the transition payments will not result in new entry and will not provide a reliability benefit to consumers as nothing is required of suppliers other than their continued existence. IECG further objects to the notion that many

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[89] Comments of Maine Parties at 12.

[90] *Id.* at note 30.

[91] Comments of Objecting Parties at 19.

generators that currently receive adequate compensation (whether through ICAP or RMR or locational forward reserves market payments) will also receive transition payments. Objecting Parties assert that transition payments will not prevent entities that earn insufficient revenue during the transition period from filing for RMR agreements and that the new availability provisions will not affect generators behavior. Objecting Parties state that were it not for the preservation of RMR agreements, parties "may decide to advance the proposition that transition payments are needed to maintain existing capacity until FCM payments begin."[92]

78. All of the above parties argue that it is inappropriate to compare the transition payments to hypothetical LICAP payments as the Commission never ruled on the LICAP proposal. Objecting Parties contend that the "less than LICAP" arguments many settling parties offer is a "wholly insufficient basis" for supporting the Settlement Agreement.[93] Maine Parties and IECG argue that a comparison to the level of LICAP payments as the likely litigated outcome is irrelevant to whether the transition payments are just and reasonable. Objecting Parties and IECG submit that LICAP payments were designed to achieve different objectives. Objecting Parties state that while LICAP rates were designed to elicit new construction, supporters make no such claim in reference to the transition payments. Moreover, Objecting Parties argue that while LICAP payments, however flawed, were based on estimated costs of new construction, there is no cost justification for the transition payments. IECG notes that the LICAP proposal would have eliminated RMR contracts, would have adjusted LICAP payments

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[92] Reply Comments of Objecting Parties at 3.

[93] *Id.* at 7-8.

for peak energy rents and held the potential for a substantial availability adjustment. Maine Parties state that transition payments are not adjusted for PER. Maine Parties and IECG argue that an analysis of comparative savings cannot provide a foundation for finding transition payments just and reasonable. IECG argues that the Commission must determine that the transition payments are just and reasonable. Maine Parties state that the appropriate comparison is to the current vertical demand curve in a locational ICAP market.

79. Objecting Parties argue that the first FCA (held in early 2008) will set a price all existing resources can expect to receive during the commitment period and thus there is no need for a bridge to FCM.

80. Maine Parties state that the transition mechanism disregards location and fails to account for Maine's capacity surplus. Maine Parties argue that this capacity surplus is unlikely to disappear during the transition period and therefore the price of capacity in Maine would likely not rise to the level of the transition payments. Maine Parties state that capacity payments should reflect the limited value of capacity during the transition period and reflect the unique circumstances of Maine.

81. Maine Parties also assert that if the Commission accepts the Settlement Agreement, it should modify the transition payments for the Maine zone to $2.00/kW-month. In the alternative, Maine Parties submit that the issue could be severed from the proceeding and set for hearing. Maine Parties state that this level would be modestly higher than prices in New York, which serve as a reasonable comparison. IECG states that it may be appropriate for some level of transition payments if there is a relationship to the value received; however, parties do not make this case. IECG states that if the Commission accepts the Settlement Agreement, it should reduce the

transition payments by 50 percent. Objecting Parties assert that for the transition mechanism to be just and reasonable, transition payments should be paid only to units needed for reliability that are not recovering going forward costs.

82. PSEG, while not opposing the Settlement Agreement, states that the capacity market will not account for the locational value of generation for five years and that the transition payments will not be sufficient to attract new market entry. Therefore, they argue, the transition mechanism will not permit generation, transmission, and demand side to compete.

83. Load Supporters, Select, Berkshire, NRG, Calpine and Lake Road all submitted comments or reply comments supporting the transition payments. Load Supporters state that the transition mechanism is an interim step to improve resource adequacy and reliability for existing suppliers until the FCM can be fully implemented. They argue that the transition mechanism provides predictable capacity payments that are not subject to the existing "all or nothing" capacity market and are not subject to the actions of other generators. Load Supporters also state that the transition mechanism removes uncertainty, provides a six month commitment period, and includes an availability adjustment if a resource fails to perform. Load Supporters state that the transition mechanism will not be subject to the potential for market power and, through the use of transition payments that are lower than the projected LICAP payments together with RMR contracts, will meet its purpose of compensating existing generation sufficiently to remain available until new generation can be constructed. They also state that the record (in particular, ISO-NE's LICAP price projections during the transition period) shows no difference in prices between Maine and the

Rest-of-Pool, and thus there is no basis to differentiate the amount of capacity payments by region, noting that RMR agreements are still paid locally during this period. Under these circumstances a locational aspect to the transition would not serve to promote increased reliability, Load Supporters contend.

84. Load Supporters also contend that the settlement balances short-term and long-term objectives during the transition period and that deconstructing the settlement to alter the transition would create implications for other aspects of the agreement. Load Supporters state that, while it is true that the full benefits of the market will be realized once FCM is fully implemented, the transition period provides superior benefits to load than either the current regime or the likely litigated outcome. Load Supporters argues the transition mechanism is superior to the Initial Decision which would have adopted a permanent solution. Under the Settlement Agreement, the transition mechanism would apply for the interim until the FCM provides a competitive market. Load Supporters describe the following benefits: the availability metric that will be in place beginning December 1, 2006; capacity resources will be committed seasonally instead of monthly; the fixed capacity payments and the resulting removal of the determination of ICR from the equation during the transition period results in certainty over the amount of capacity load will purchase; and capacity payments are not targeted to financially distressed suppliers.

85. Load Supporters further state that the transition payments have been shown to be less than the capacity payments under the Initial Decision, and that Maine is not making appropriate comparisons. They note that under the status quo, load will be exposed to capacity payments that may approach the $6.66/kW-month defi-

ciency rate due to forecasted load growth. Load Supporters also state that the transition payments are well below the estimate for the cost of new entry and are premised on the assumption that over the long term, capacity payments should be the cost of new entry.

86. Load Supporters state that Maine Parties have not made arguments that justify different treatment during the transition and states that all of New England has a current capacity surplus, not just Maine. They state that Maine Parties have incorrectly relied on congestion charges in the energy market as a basis for stating that capacity payments should be reduced to $2.00 per kilowatt-month for Maine, and for assuming that the rest of New England, which is not capacity deficient, will require that an amount of capacity be imported from Maine, sufficient to create a binding transmission constraint.

87. Lake Road states that failure to implement the Settlement Agreement in total, including the transition payments, would have a number of negative effects, including: exacerbating the need for RMR agreements; increasing the likelihood of generator bankruptcies; failing to provide the incentive for the development of infrastructure; and disrupting the functioning deregulated market in New England. Further, Lake Road states that the transition payments are critically important and will provide a badly-needed solution in the short-term. Similarly, Capacity Suppliers state that it is not an option to spend nothing on capacity during the period covered by the transition mechanism.

88. American National Power argues that Objecting Parties' claims that generators should not be paid for capacity conflicts with the Commission's reasoning directing the development of LICAP; *i.e.*, that generators in designated congestion areas be appropriately compensated for reliability. It further states that Objecting Parties' com-

plaint that the transition payments are "money for nothing" does not acknowledge that capacity is a legitimate product for which existing generators should be paid. American National Power also states that the Commission has distinguished the locational forward reserves market from the capacity market and recognizes that the capacity market ensures there is adequate generating capacity installed on the system. It also takes issue with the conclusions made by Maine Parties that there is a relationship between the energy market and binding transmission constraints in the capacity market. American National Power, as well as Calpine, state that without a technical demonstration of a binding capacity constraint, for which no evidence was presented, a capacity price reduction for Maine is not justified.

Commission Conclusion

89. While the Commission may not consider the transition payments ideal as a single market design element, when considered as part of the larger Settlement Agreement, we find (consistent with the second approach of *Trailblazer*) that they serve as a reasonable transitory mechanism that enables the New England region to shift to the FCM. We note that the FCM incorporates many of the proposed features of alternatives presented at oral argument. We find that the transition payments are a just and reasonable component of the overall package embodied in the Settlement Agreement because: (1) based on record evidence from the hearing, the payments fall within the reasonable range of capacity prices, and contesting parties are in no worse position under the Settlement Agreement than they would be through continued litigation; (2) in the first years, the payments are less than the cost of new entry, accurately reflecting market conditions; and (3) the payments result in just and reasonable rates for existing generators.

90. Over the course of the 10-month hearing in this proceeding, numerous parties filed alternative demand curves to the curve proposed by ISO-NE. The Commission never ruled on the justness and reasonableness of that demand curve or any of the other demand curves proposed in the hearing (although the Initial Decision did adopt ISO-NE's proposal). Nonetheless, for the purposes of addressing the Settlement Agreement as a just and reasonable package, and establishing the justness and reasonableness of the transition payments as part of that package, we can analyze the price projections under the proposed demand curves that were entered into evidence in the hearing and compare them to the transition payments. As we noted above, "[a] just and reasonable rate is not a product of any single formula, but is instead a rate within a broad ambit of various rates which may be just and reasonable."[94] We disagree with arguments that the Commission cannot compare the transition payments to the potential rates that would have resulted from continued litigation over the LICAP mechanism. As we discuss above with regard to our standard of review, under the second *Trailblazer* approach, the Commission must find that contesting parties would be in no worse position under the settlement than if the case were litigated. Comparing the transition payments to the likely outcome of litigation is the most reasonable approach for evaluating this aspect of the Settlement Agreement.

91. The record evidence shows a range of rates that could have resulted from continued litigation. In particular, it is useful to look at the projected prices for Maine and Northeastern Massachusetts/Boston under the de-

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[94] *See Belco Petroleum Corp. v. FERC*, 589 F.2d 680, 689 (D.C. Cir. 1979), *citing Permian Basin Area Rate Cases*, 390 U.S. 747, 767 (1968); *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 602 (1944); *FPC v. Natural Gas Pipeline Co.*, 315 U.S. 575, 585-86, (1942).

mand curve proposed by Maine and Vermont load representatives (one of the lower demand curves) and ISO-NE's proposed demand curve. While other demand curves were proposed at the hearing, the parameters of those curves would have produced prices that were either much higher or much lower. The Maine/Vermont and ISO-NE curves provide a narrow range of rates that provide a reasonable basis for comparison to the transition payments.

92. In direct testimony filed February 10, 2005, ISO-NE witness David LaPlante provided a series of price estimates, for a variety of scenarios, using the ISO-NE-proposed demand curve.[95] ISO-NE projected prices for each of five LICAP regions previously approved by the Commission: Southwest Connecticut (SWCT), Rest of Connecticut, Northeast Massachusetts/Boston (NEMA/Boston), Maine and the Rest of Pool. ISO-NE developed price estimates for Maine that ranged from $2.29/kW-month in 2007 to $4.04/kW-month in 2010; prices for NEMA/Boston were the same.[96]

93. In the same exhibit, ISO-NE also projected capacity prices under a demand curve advocated by Maine and Vermont load representatives.[97] ISO-NE projected prices for Maine under that curve that ranged from $1.91/kW-month in 2007 to $2.53/kW-month in 2010; prices for NEMA/Boston were the same.

94. James Daly, witness for a coalition of parties, including the Attorney General of Massachusetts (AG Mass), NSTAR and The Energy Consortium, also developed a

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[95] Exhibit No. ISO-24.

[96] *Id.*

[97] The Maine Public Utilities Commission, Maine Public Advocate, Vermont Department of Public Service and the Vermont Public Service Board.

series of price projections using ISO-NE's demand curve. He first provided projections in supplemental answering testimony, filed January 28, 2005. On March 16, 2005, Mr. Daly updated his price projections to reflect an increase in the installed capacity requirement as approved by the NEPOOL Participants Committee.[98] Mr. Daly's price projections for Maine ranged from $7.63/kW-month in 2007 to $16.16/kW-month in 2010; prices for NEMA/Boston were the same.[99] Mr. Daly argued that the net cost of ISO-NE's LICAP proposal was $14.5 billion.[100] Maine Parties and Vermont argued that, using the updated installed capacity requirement, "cost[s] will rise to $1.2 billion and $7.3 billion for Maine and Rest of Pool, respectively, for a five-year period."[101] In their Reply Brief, Maine Parties and Vermont argued that New England consumers could pay "as much as $6 billion in LICAP charges" during the first three years of ISO-NE's proposal.[102]

95. In Attachment 6 to the Settlement Agreement, ISO-NE witness David LaPlante provided updated capacity price projections using the demand curve approved in the Initial Decision, which is identical to the ISO-NE-proposed demand curve for which Mr. LaPlante provided

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[98] The installed capacity requirement is established annually via the NEPOOL stakeholder process, approved by a vote of the NEPOOL Participants Committee and filed with the Commission under section 205 of the FPA.

[99] Workpaper for Exhibit No. AG Mass-23

[100] Exhibit No. AG Mass-23 at 3.

[101] Initial Brief of the Maine Public Utilities Commission, the Maine Public Advocate, the Vermont Department of Public Service and the Vermont Public Service Board at 32.

[102] Reply Brief of the Maine Public Utilities Commission, the Maine Public Advocate, the Vermont Department of Public Service and the Vermont Public Service Board at 5.

projections in February 2005. Mr. LaPlante relied on updated assumptions, including the level of installed capacity requirement approved by the Commission for the 2005/2006 power year, as well as installed capacity requirement projections contained in the most recent ISO-NE Regional System Plan. Mr. LaPlante's price estimates for Maine ranged from $4.13/kW-month in 2007 to $7.84/kW-month in 2010; prices for NEMA/Boston were the same.[103]

96. These most recent price projections, using the ISO-NE demand curve, exceed those made by Mr. LaPlante in February 2005. Therefore, it is reasonable to assume that had Mr. LaPlante also updated the price projections for the demand curve proposed by Maine and Vermont load representatives, those projected prices would have increased in similar magnitude from the February 2005 projections.

97. This record evidence indicates that the cost of the transition payments to Maine and Massachusetts customers under the Settlement Agreement would be less than the costs of ISO-NE's proposed demand curve. In its Initial and Reply Briefs, Maine Parties[104] made various assertions with regard to the total costs of LICAP to Maine customers, projecting the costs at anywhere from $734 million to $1.2 billion through 2010. In his affidavit, Maine Parties' witness Thomas Austin submits that the transition payments as proposed by the Settlement Agreement "will cost Maine consumers about $300 mil-

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[103] Settlement Agreement, Attachment 6.

[104] In briefs on the Initial Decision, Maine Parties were joined by the Vermont Department of Public Service and the Vermont Public Service Board. Both the Vermont Department of Public Service and the Vermont Public Service Board are parties to the Settlement Agreement. They filed in support of the Settlement Agreement as members of Load Supporters.

lion over the transition period," which ends in 2010.[105] By the Maine Parties' own admission, the transition payments will impose far fewer costs on Maine customers than the price projections Maine Parties referenced in its Initial and Reply Briefs.

98. An examination of the various price projections illustrated above, using ISO-NE's proposed demand curve as well as Maine Parties' and Vermont's demand curve, shows a range of prices that could have resulted from continued litigation. The chart below shows projections for Maine and for NEMA/Boson, with the transition payments included for comparison:

Range of Project Prices – Maine $/kW-month

	2007	2008	2009	2010
LaPlante - ME & VT Curve (Feb. 2005)*	1.91	1.96	1.64	2.53
LaPlante - ISO-NE Curve (Feb. 2005)	2.29	2.36	4.44	4.04
Transition Payments	3.05	3.05	3.75	4.05
LaPlante - ISO-NE Curve (March 2006)	4.13	5.14	6.39	7.84
Daly - ISO-NE Curve (March 2005)	7.63	10.21	14.26	16.16

*Not updated to reflect current assumptions.

[105] Affidavit of Thomas D. Austin at 9, filed with Comments of the Maine Parties Contesting the Proposed Settlement, March 27, 2006.

Range of Project Prices – NEMA/Boston $/kW-month

	2007	2008	2009	2010
LaPlante - ME & VT Curve (Feb. 2005)*	1.91	1.96	1.64	2.53
LaPlante - ISO-NE Curve (Feb. 2005)	2.29	2.36	4.44	4.04
Transition Payments	3.05	3.05	3.75	4.05
LaPlante - ISO-NE Curve (March 2006)	4.13	5.14	6.39	7.84
Daly - ISO-NE Curve (March 2005)	7.63	10.21	14.26	16.16

*Not updated to reflect current assumptions.

99. As the above data indicate, the record evidence shows that the transition payments fall well within the range of capacity prices projected using the demand curve proposed by ISO-NE, as well as the demand curve proposed by Maine Parties and Vermont during the hearing. The Commission notes that projected prices using the Maine and Vermont-proposed demand curve do not reflect the most recent installed capacity requirement and other updated assumptions. Since those updated assumptions produced a sharp increase in prices under the ISO-NE-proposed demand curve, it is reasonable to assume that the initial projections for the Maine and Vermont-proposed demand curve are too low and would increase in a similar manner. Thus, the transition payments fall at the very low end of this price range.

100. Taken as a whole, we conclude that this evidence establishes the justness and reasonableness of the transition payments as a component of the overall package represented by the Settlement Agreement. Not only does the evidence show that the transition payments fall within the "range of reasonableness," as discussed above, but the evidence also leads us to conclude (consistent with the second *Trailblazer* approach) that those objecting to the settlement would not reach a more favorable

result through continued litigation. The record evidence shows that even had the Commission, in continued litigation, adopted elements from other, lower demand curves proposed at hearing, the transition payments would still be comparable if not significantly lower. Taking into account the expense of continued litigation and its attendant uncertainty, we conclude that contesting parties "would be in no worse position under the terms of the settlement than if the case were litigated."[106]

101. Moreover, the proposed transition payments are significantly less than the estimated cost of new entry of a new peaker, a type of plant whose capital costs are lower than most, if not all, other plants. Thus, the payments are likely to be significantly lower than a cost-of-service payment for most, if not all, new generators. As noted above, the Settlement's proposed transition payments would be set initially at $3.05/kW-month and rise to $4.05/kW-month for 2010. These payments are significantly lower than the $7.50/kW-month CONE used to begin the FCM auction, which, as discussed below, we find reasonable. Thus, the payments are well within the "range of reasonableness."

102. Additionally, the transition payments are reasonable rates for existing generators until the FCM begins. Comments that the transition payments are unreasonable and inappropriate because they will not provide the incentive for new entry ignore that one of the Commission's stated goals in this proceeding is to ensure that existing generators are appropriately compensated.[107]

103. Finally, the transition payments will require a long-term commitment and will be more closely tied to the

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[106] *Trailblazer*, 87 FERC ¶ 61,110 at 61,339.

[107] April 25 Order at P 37; June 2 Order at P 40-43, 49-52; *Devon Power LLC*, 109 FERC ¶ 61,154 at P 65-67 (2004).

availability of a unit, both significant improvements over the existing capacity market (status quo) and the LICAP proposal as approved in the Initial Decision. First, the transition payments will be adjusted to account for unit performance during periods of high demand. Transition payments will also be adjusted by an EFORd score that is weighted according to on-peak hours, seasonal peak hours, and shortage hours (including certain periods of system-wide emergency operations or actions).[108] Second, the commitment period for capacity resources consists of two six-month seasonal periods (section VIII.H), as compared to the monthly period in the current capacity market. Third, during the transition period, suppliers may partially de-list or export their units (section VIII.F), an attribute the Commission previously stated would be desirable.[109]

104. The existing capacity market does not provide these features. The current market only adjusts capacity payments for average unit availability (unforced capacity (UCAP)), while the transition period will provide an adjustment to transition payments for suppliers that do not perform that is targeted more effectively to periods of system stress. We also find that the longer commitment period for capacity resources is superior to both the status quo and to ISO-NE's LICAP proposal. Under the current ICAP market, the commitment period is monthly; the commitment period under ISO-NE's LICAP proposal was also monthly. During the transition period, supply resources must commit to a six-month seasonal supply of capacity. Taken together, these provisions increase the stability of the market during the transition period and add certainty and price stability for load cus-

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[108] Settlement Agreement, section VIII.D

[109] *New England Power Pool*, 100 FERC ¶ 61,287 at P 110 (2002).

tomers. We find that these features provide enhanced reliability and customer protection that is superior to the existing ICAP market, which we have found to be unjust and unreasonable.

105. Maine Parties argue that the transition payments fail to account for locational differences in capacity levels, and that Maine should pay a lower transition payment because it has a surplus of capacity. However, record evidence does not support altering the transition payment for Maine based on its capacity surplus. The most recent price projections provided by Mr. LaPlante exhibit little to no variability in capacity prices across New England regions for the period covered by the transition mechanism. Furthermore, in areas where import constraints do currently exist, RMR agreements have been approved, and the costs associated with those payments are paid locally.[110] Therefore, for this limited period, it is reasonable to not include a locational feature in the transition mechanism. The locational feature in the FCM, which we address below, appropriately addresses on a long-term basis issues regarding payments to capacity in constrained regions.

106. We also reject Maine Parties' request that we sever the issue of what level of transition payment Maine should pay. As we concluded above in our discussion of the standard of review, severance is not appropriate in this case because the Settlement Agreement provides a capacity market construct (including a transition period) that will apply throughout New England. Moreover, as Settling Parties note in their explanatory statement, the level of transition payments for the entire region were negotiated at arms length among all of the Settling Par-

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[110] *See* Explanatory Statement in Support of the Settlement Agreement at 39.

ties.[111] Severing the amount one state will pay would undoubtedly affect that negotiated amount for all parties.

107. The Commission will not reduce the level of the transition payments by 50 percent as suggested by IECG. IECG arrives at 50 percent without demonstrating why that is the appropriate level. Also, the transition payments are a fundamental component of the Settlement Agreement.

108. Finally, we address arguments with regard to the relationship between the Settlement Agreement and the currently-approved RMR agreements below.

2. FCM Design

a. Alternative Price Rule

109. The settlement provides for an alternative price rule that will reset the clearing price under certain conditions. This rule allows load to self-supply their own capacity, but removes the incentive to do so for the purpose of depressing capacity prices. The rule applies when at least some of the offers from new capacity or imports are below .75 times CONE and the Market Monitor concludes that such low offers are not consistent with long run average costs, opportunity costs, or other reasonable economic measures. Capacity submitting such bids is deemed to be "out-of-market." When any submitted bids are deemed out-of-market, the capacity clearing price will be reset when the following conditions are met: 1) new capacity is needed, either system-wide or in an import-constrained zone; 2) there is adequate supply in the auction; and 3) at the auction clearing price, purchases from out-of-market capacity are greater than the required new entry. If these conditions are met, the clearing price for the applicable capacity zone will be set

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[111] *Id.*

to the lower of 1) the price at which the last bid from new capacity was withdrawn, minus $0.01 or 2) CONE.

110. Objecting Parties and IECG argue that the alternative price rule should be rejected because it maintains an artificial price support for incumbents. IECG argues that the alternative price rule interferes with competition between existing suppliers and self-supply by load serving entities. IECG argues that this rule prevents long-term contracting opportunities from effectively competing in the auction process and thus discourages long-term contracting by load serving entities. Objecting Parties argue that the sole purpose of the alternative price rule is to maintain a LICAP level of quantity and price support in the market, which reflects the unbalanced negotiating positions among the parties rather than any rational market mechanism.

111. Capacity Suppliers respond that the alternative price rule does not restrict competition, but rather, curbs the exercise of load's monopsony power. Capacity Suppliers assert that without this rule, there is no way to restrict load from submitting artificially reduced bids for new capacity, thus driving clearing prices to zero. Capacity Suppliers' witness Stoddard states that the rule does not interfere with the ability of load to contract bilaterally, but that it prevents loads that may control a small amount of new capacity needed to meet load growth—perhaps one or two percent—from setting the clearing price for the remaining 98 to 99 percent of capacity. Mr. Stoddard argues that when new resources that are under contract to load or otherwise indifferent to the capacity clearing price submit bids below the average cost of new entry, they may be able to set the clearing price; in these instances, the auction price would inaccurately be signaling that there is no need for new generation, while contract market prices would be signaling

that there is a need for new generation. ISO-NE contends that, in instances where new supply is required to meet the Installed Capacity Requirement, the alternative price rule prevents the price from dropping to zero. ISO-NE contends that the alternative price rule sets a methodology that directly ties the clearing price to an actual bid by new capacity or CONE and prevents price volatility, thus providing consumers with price predictability and rate stability.

112. Load Supporters assert that the alternative price rule will exclude bids that do not represent actual costs and thus is designed to ensure that prices over the long run will approximate the true cost of new entry. Load Supporters assert further that as long as a self-supplied resource bids its true costs, it can set the auction clearing price. Load Supporters argue that the rule helps to ensure that the competitive cost of new entry sets the clearing price when entry is needed, and, therefore, provides incentives for investment in new capacity.

Commission Conclusion

113. We find that the alternative price rule is a reasonable provision of the settlement because it helps to ensure that capacity prices will reflect the price needed to elicit new entry when new capacity is needed. In the absence of the alternative price rule, the price in the FCA could be depressed below the price needed to elicit entry if enough new capacity is self-supplied (through contract or ownership) by load. That is because self-supplied new capacity may not have an incentive to submit bids that reflect their true cost of new entry. New resources that are under contract to load may have no interest in compensatory auction prices because their revenues have already been determined by contract. And when loads own new resources, they may have an interest in depressing the auction price, since doing so

could reduce the prices they must pay for existing capacity procured in the auction. If the owners of these two categories of resources control more new capacity than the amount of new capacity needed in a capacity zone, their low bids could artificially depress the price in the FCA.

114. To address this potential problem, it is reasonable for the Market Monitor to review offers from new capacity that appear to be unreasonably low. And if the Market Monitor determines that a low offer is not economically justified, it is reasonable to reset the clearing price to a level that would be expected in a competitive market that requires new capacity. The reset price under the alternative price rule is such a price. The alternative price rule provides two options for establishing a reset price. One option is CONE; it is reasonable to expect that the market price would normally approximate the estimated cost of new entry when new entry is needed. Under the alternative price rule, the reset price would never exceed CONE. But under the second option, the price would be less than CONE in those instances when an in-market source of new capacity has indicated through its bid that it is willing to supply capacity at a price less than CONE. In these instances, it is reasonable to reset the price at a level slightly below the last bid from in-market new capacity that has withdrawn from the auction. Furthermore, under section IX of the Settlement Agreement, ISO-NE will provide an informational filing 90 days prior to the conduct of each FCA; that informational filing will identify any Market Monitor conclusions concerning the acceptability of bids in the FCA, allowing the Commission to review the Market Monitor's actions.

115. We disagree with Objecting Parties and IECG that the alternative price rule would maintain an artificial

price support for incumbents; rather, we agree with Capacity Suppliers that the rule would ensure that new capacity, when needed, will receive a reasonable price. We also disagree with IECG that the rule would discourage long-term contracting and interfere with competition between existing suppliers and self-supply by load serving entities. Rather, we agree with Load Supporters that the rule would not preclude self-supply or bilateral contracting. The rule would not eliminate the value of self-supplying or contracting to create a hedge against the uncertainty of auction clearing prices. The rule would merely help to ensure that loads do not use self-supply to artificially suppress the auction's clearing price below the price needed to elicit new entry when new entry is needed.

b. Locational Feature

116. In addition to its concerns regarding the lack of a locational element in the transition period, Maine Parties also express concerns regarding the locational feature of the FCM. As noted above, under the locational feature included in the Settlement Agreement, ISO-NE will determine any separate capacity zones prior to each auction based on its identification of transmission constraints that may bind. This compares to the LICAP proposal, under which the capacity zones would be permanently established in the tariff and would not change prior to each auction absent a tariff change.

117. Specifically, Maine Parties argue that the determination by ISO-NE of whether binding constraints exist (which will then result in separate import constrained zones) is inferior to allowing actual price separation to occur as part of the auction process. In particular, Maine Parties argue that the administrative determination will be made with incomplete information, and could be influenced by entities with greater resources. Maine

Parties also argue that this process could result in the region purchasing capacity that is not deliverable to the import-constrained region, leading to higher prices (since more capacity is being paid than can be delivered). Furthermore, Maine Parties contend that a pre-determined conclusion that a constraint will or will not bind is unduly rigid and suppresses market forces that would ordinarily determine the locational value of capacity on their own. Maine Parties conclude that "[t]he failure to model import constraints in the auction runs counter to the Commission's core interest of ensuring price separation to value capacity properly in import-constrained zones."[112]

118. In reply, Load Supporters argue that the Settlement Agreement properly determines the need for separate capacity zones before the auction, and that much of the agreement hinges on this feature. Load Supporters contend that five separate auctions would be inefficient where objective criteria apparent before the auction show no need for the separate zones. Additionally, Load Supporters assert that establishing ISO-NE's determination and criteria in advance allows load to take action to minimize the impact of separate, smaller capacity zones. Load Supporters state that changing this aspect of the settlement could disturb the delicate balance reached in the package as a whole. Furthermore, in response to Maine Parties' suggestion that the locational element could result in the purchase of capacity that is not deliverable, Load Supporters state that the Settlement Agreement includes explicit provisions to maintain local resource adequacy and reliability in a more precise manner than would Maine Parties' suggested modification.

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[112] Comments of Maine Parties at 17.

119. ISO-NE, in its reply, explains that the locational mechanism in the Settlement Agreement was a compromise crafted to bring together parties who favored either a locational capacity market or a regional capacity market. ISO-NE states that the need for a locational capacity market is critical to provide an incentive for the right mix of generation in the right locations, and the approach in the settlement was negotiated to ensure that there would be a locational element in the market when and where required. Furthermore, ISO-NE notes that export constraints will be modeled through the auction, making Maine Parties' concern only directed at import constraints. According to ISO-NE, while always including a separate zone in the auction might be a better approach in theory, the approach in the Settlement Agreement will achieve the same result by identifying the need for new capacity or transmission inside an import-constrained zone and then properly pricing it. Additionally, ISO-NE and Load Supporters argue that the zonal determinations will not be subject to undue influence, since the ISO will be required under the settlement to make an informational filing with the Commission, which parties can then challenge.

120. Finally, ISO-NE contends that Maine Parties are incorrect that more capacity may be purchased than can be imported into the constrained zone because under the settlement's "before-the-fact" determination process, the amount of existing capacity and capacity that is committed to be constructed is compared to the capacity needed within the zone (given assumed transmission) and if there is sufficient capacity, no separate zone is modeled. Since the calculation is done each year, changed circumstances are taken into account, and only the retirement of a unit during the auction (without a purchase of replacement capacity) could result in an incorrect calculation. ISO-NE states this scenario is unlikely and is addressed by

the retirement rules and market mitigation thresholds under the ISO-NE tariff.

121. National Grid, also in reply, argues that the Settlement Agreement resolves locational concerns more effectively than the LICAP mechanism because it ties the creation of zones directly to the actual current location of load pockets, and is performed on an annual basis to reflect current system conditions, instead of creating rigid and inflexible zones that are changed only with difficulty. Furthermore, it contends that Maine Parties' assertion that ISO-NE will determine the zones by "administrative fiat" is without merit, because ISO-NE will use an objective technical test to identify the zones, and will use local sourcing requirements (*i.e.*, the amount of capacity that must be obtained within each zone) based on a well-defined reliability analysis and a methodology for determining transfer limits between regions that the parties have previously uniformly supported.[113] Additionally, National Grid contends that Maine Parties' proposal to alter the locational feature will present market power concerns, since pre-established zones (such as those in the LICAP proposal) present more of an opportunity to manipulate participation in the auction to force the predefined transmission constraints to bind and create price separation, while determining the zones before the auction based on objective factors analyzing the actual state of the system will minimize such opportunities. Finally, National Grid argues that altering this feature could cause a collapse of the settlement.

Commission Conclusion

122. We will accept the locational feature of the FCM, which (as we explain here) contributes to the overall justness and reasonableness of the Settlement Agreement as

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[113] Reply Comments of National Grid at 4-5.

a package and satisfies the directive in prior Commission orders that the capacity market take into account location. Transmission constraints in New England can restrict the ability to deliver energy from some locations to others, and a market design for capacity should reflect transmission constraints to send correct price signals for investment. We believe that the settlement provides for a means to recognize transmission constraints that is, on balance, reasonable in light of competing considerations.

123. Under the settlement, separate capacity zones would be established for each yearly FCA in those instances when the ISO determines in advance that transmission constraints are likely to bind. The Maine Parties argue that determining zones in advance, as proposed in the settlement, is inferior to allowing price separation to occur as part of the auction process. In principle, there may be advantages to the Maine Parties' approach, but the settlement's approach will reduce the incentive to exercise market power in the capacity market. We agree with National Grid that if auction results were used to force local capacity zones/local auctions, as Maine Parties' propose, sellers of capacity would have the incentive to withhold capacity to create price separation and separate capacity zones where they are not necessary.[114] These constraints would bind only because of the exercise of market power, and not because of actual physical limitations arising from competitive market conditions. The locational feature of the Settlement Agreement, in contrast, will be based on an objective analysis of actual transmission system constraints.

124. Therefore, we accept the locational feature of the FCM. We note that the settlement provides for the ISO's Market Monitor to post a report analyzing the op-

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[114] *See* Reply Comments of National Grid at 7.

erations and effectiveness of the FCM no later than 180 days after the second FCA is conducted, as well as annually in its annual markets report. In these reports, the Market Monitor should include an evaluation of the locational element.

c. Level of CONE/"Collar"

125. Under the Settlement Agreement, the beginning price for each FCA will be twice CONE (or $15.00/kW-month), with the value of CONE for the initial FCA set at $7.50/kW-month. In subsequent auctions, CONE will be based on preceding values of CONE and preceding auction clearing prices.

126. Objecting Parties argue that the initial CONE of $7.50/kW-month is excessive and should be set below $7.00/kW-month. Objecting Parties assert that the combination of an excessive CONE and the price floor established via the collar mechanism will result in load paying excessive capacity charges even in a surplus situation. Objecting Parties note that capacity payments will be netted against reserves payments from the locational forward reserves market. Reserves payments are capped at $14/kW-month. Objecting parties argue that, given that the beginning price for capacity will be $15.00/kW-month (two times CONE), there is the possibility that reserves will clear at a lower price than capacity, meaning qualified locational forward reserves markets resources could have to take a financial loss to provide locational reserves.

127. Maine Parties argue that setting the initial CONE at $7.50/kW-month is too high, particularly for Maine, which has a surplus of generation and limited export capability. Maine Parties assert that the CONE does not reflect the lower cost of new entry in Maine relative to other locations in New England. Maine Parties cite

LICAP testimony from ISO-NE witness Reed, who determined that several inputs into the totaled installed costs of generation were higher in Southwest Connecticut than in Maine.[115] Maine Parties argue that, in the LICAP proceeding, ISO-NE proposed an estimated benchmark cost of capacity for Maine that was $1.00/kW-month lower than Southwest Connecticut. Thus, Maine Parties assert that a just and reasonable initial CONE for Maine would be $6.50/kW-month. Maine Parties also argue that the collar mechanism will keep prices artificially high.

128. Capacity Suppliers and ISO-NE argue that neither Objecting Parties nor Maine Parties provide analyses or cite record evidence to support an alternative value for the initial CONE. Capacity Suppliers submit that the primary purpose of CONE is to indicate the auction's beginning price; actual clearing prices will reflect the market for capacity not CONE. Capacity Suppliers and ISO-NE contrast the proposed $7.50/kW-month level of initial CONE with the estimated cost of new capacity derived by ISO-NE witness Reed during the LICAP proceeding—$7.27 in Maine, $7.70 in Rest of Pool, and $8.16 in NEMA/Boston. Capacity Suppliers assert that this record evidence substantiates the $7.50 CONE estimate, which is for the 2010/11 power year.

129. Load Supporters submit that the settling parties made great efforts to balance the risks between resource

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[115] ISO-NE witness John J. Reed derived the following values for the estimated costs of capacity for a benchmark peaking unit (*see* Exhibit No. ISO-3 in Docket No. ER03-563-030):

LICAP Region	NEMA/ Boston	SWCT	Rest of Connecticut	Maine	Rest of Pool
$/Kw-year	$97.87	$99.16	$96.52	$87.22	$92.34
$/kW-month	$8.16	$8.26	$8.04	$7.27	$7.70

suppliers and load so that the long-term CONE could assure a steady stream of new competitors willing to offer capacity at the lowest reasonable cost. Load Supporters assert that altering the initial value for CONE would disrupt the settlement's delicate equilibrium, and may precipitate its collapse.

Commission Conclusion

130. The Commission will not modify the initial value of CONE proposed in the Settlement Agreement. We find that the $7.50/kW-month CONE is a reasonable estimate of the cost of new entry and basis for the beginning price in the FCM auctions, and we believe it is supported by substantial evidence in the record. For example, the $7.50/kW-month CONE is at the lower part of the range of the estimated benchmark costs of capacity produced by ISO witness Reed at the hearing in this proceeding. Further, Capacity Suppliers' witness offers substantial evidence that, after adjusting Mr. Reed's estimates for inflation over four years to 2010, the $7.50/kW-month level of CONE would be lower than all of Mr. Reed's estimates.[116] Additionally, the $7.50/kW-month figure is not a substantial increase from the existing $6.66/kW-month deficiency charge currently in place in the ICAP market and approved by the Commission in 2002, given inflation and increases in the cost of capacity.[117] Neither Maine Parties nor the Objecting Parties offer any evidence as to why their suggested modifications provide a more reasonable estimate of the cost of new entry.

131. With regard to the issue raised by Objecting Parties' regarding the impact of the FCM on the locational

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[116] Supplemental Affidavit of Robert B. Stoddard at 3, Filed with Reply Comments of Capacity Suppliers.

[117] *See New England Power Pool and ISO New England, Inc.*, 100 FERC ¶ 61,287 at 62,277-78 (2002).

forward reserve market, the Commission notes that, while $15.00/kW-month is the initial bid price (representing two times CONE), the prices in the descending clock auction will descend until the market clears. Subsequent values of CONE will be "mathematically calculated using the clearing prices of previous auctions"[118] and thus the beginning prices in subsequent FCAs will reflect the prices needed to elicit supplies to serve projected demand. Additionally, prices paid to capacity suppliers will be reduced via the peak energy rent deduction and availability metric. We expect that these provisions will appropriately address Objecting Parties' concerns. We note that in the locational forward reserves market proceeding,[119] ISO-NE indicated that the locational forward reserves markets settlement rules would accommodate the design of any successor capacity market in this docket. We expect ISO-NE to carefully observe prices in the locational forward reserves markets and FCM markets and to file to correct any problems of overlap.

132. We will not grant Maine Parties' request to reduce CONE for Maine alone. First, we note that CONE is only a starting point for the auction, and changing CONE for Maine alone will not change the actual cost of new entry in Maine. Since it is simply a beginning point for the auction, CONE will not necessarily establish the market clearing price in all FCAs. Moreover, we find that a single value for CONE is just and reasonable, since the FCM is a region-wide construct with a locational element when transmission system conditions warrant. Additionally, the $7.50/kW-month CONE differs only slightly from the $7.27/kW-month estimated cost of capacity for a benchmark peaking unit entered into evidence by ISO-

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[118] Explanatory Statement to Settlement Agreement at 26.

[119] *ISO New England, Inc.*, 115 FERC 61,175 (2006).

NE witness Reed in the hearing below, even without updating Mr. Reed's figure to reflect inflation and increased fuel costs.[120] Furthermore, Maine Parties do not address how different CONEs for Maine and for the rest of New England would operate in practice with respect to a single clearing auction.

d. Definition of "New Capacity"

133. Under the Settlement Agreement suppliers that undertake new investment in existing resources (*i.e.*, capacity that is considered to be existing capacity) to increase output may have capacity reclassified as new capacity. A previously existing resource shall be considered new capacity if the supplier undertakes new investment such that: (1) resource output is increased by the greater of 40 megawatts or 20 percent of Summer Seasonal Claimed Capability[121]; (2) the resource is repowered at a rate equal to or greater than $200 (plus appropriate cost escalation) per net kilowatt installed project cost; (3) the resource is upgraded to comply with environmental regulations or permits at a rate equal to or greater than $100 (plus appropriate cost escalation) per net kilowatt installed project cost. The Settlement Agreement also contains provisions to classify incremental capacity additions as new capacity.

134. Objecting Parties argue that because existing suppliers have both the incentive and ability to withhold capacity, it is important that only "new" resources be allowed to set the auction clearing price. While Objecting

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[120] *See* Exhibit No. ISO-3

[121] The Seasonal Claimed Capability rating of a generating unit is the maximum dependable load carrying ability, in megawatts the unit and represent the MW value of the resource used in the capacity market. All resources within New England must perform capability audits. Capabilities are calculated for winter and summer.

Parties acknowledge that there is probably some reasonable uprate threshold for declaring existing capacity "new," they argue that the greater of 20 percent or 40 megawatt threshold included in the settlement is too low. Objecting Parties argue that requiring 100 percent or more is more appropriate; with 100 percent a resource owner would need to add a megawatt of truly new capacity for every megawatt of existing capacity that would be withdrawn from the market and reclassified as "new."

135. Objecting Parties also argue that the ability of all imports to qualify as new capacity is an additional flaw. Objecting Parties contend that allowing imports to set capacity prices above the CONE creates an unnecessary opening for the exercise of market power, and increases the probability that existing resources will set the clearing price. Objecting Parties argue that enabling existing resources outside the pool to set high clearing prices creates a gaming opportunity for existing resource owners to export and then import a corresponding amount as new for the purpose of influencing prices. All imports, they argue, other than from new transmission or new generation construction, should be treated as "existing" resources in the FCA.

136. Load Supporters, in their reply comments, argue that the 20 percent/40 megawatt threshold promotes competition. Load Supporters and Capacity Suppliers assert that repowering brownfield sites may be completed more quickly and at a lower cost than new construction because the site is already permitted, licensed, and developed for generation use. Load Supporters argue that the FCM is reasonably designed to enable existing resources to improve their sites quickly, to provide substantial value at least-cost to load, and to improve capacity resource reliability and adequacy where needed. Capacity Suppliers state that settling parties

agreed that sending market signals to existing units to incur upgrade costs, when economic and efficient, is appropriate. ISO-NE contends that the Settlement Agreement is premised on the notion that an uprate of the sizes identified would require "extremely significant" investment. Load Supporters add that upgrades of at least 20 percent are unlikely to be possible without some period of de-listing. ISO-NE submits that new investment in existing units is precisely the new entry the FCM hopes to attract. ISO-NE states that an uprate of that size would further require new environmental permits, new interconnection and major additions to or replacements of existing components. ISO-NE submits that market rules will assure that capacity from these re-powerings will be unable to exercise market power. NRG argues that investors will not fund output increases without finding that the capacity market will support that investment.

137. In reply, Capacity Suppliers also argues that the ability of imports to set the clearing price was designed to increase competition between proposed new generation and imports and should serve to reduce the FCM clearing price. ISO-NE argues that if external generation is ineligible to set the price, it will sell its output elsewhere.

Commission Conclusion

138. The Commission will not direct the settling parties to reconsider the threshold used to reclassify existing capacity as new capacity. The Commission finds that the threshold provision to which the Objecting Parties refer provides incentives to attract more supply to New England because it will encourage existing suppliers to expand their facilities. We further find that the level of the 20 percent/40 megawatt threshold is sufficient to provide incentives for significant additions to capacity

levels, while preventing existing capacity from being reclassified as new capacity by means of minor additions. We note that both Load Supporters and Capacity Suppliers argue that investment in existing capacity may be more cost efficient than new construction as well as quicker to come online. Results of recent ISO-NE analyses, presented in the 2005 Regional System Plan, show that "New England will likely face an increased risk of operating with less capacity than needed by 2008."[122] The 2005 Regional System Plan further states that results indicate that the region "will not have sufficient capacity to meet the IC Requirement in the 2008 to 2010 timeframe, depending on load growth, weather conditions, generator performance and attrition, and the conditions in specific load pockets, such as Connecticut." Given these projections and that new generation requires two to four years to be built, increased output from existing resources could provide important reliability protection. The Commission thus accepts the 20 percent/40 megawatt threshold agreed to by settling parties as an appropriate means for attracting additional capacity.

139. We note that the Objecting Parties do not oppose the provision generally; rather they propose an alternative level (100 percent) as they believe the 20 percent/40 megawatt level is too low. The Commission finds that a 100 percent threshold level is too high. One of the benefits of the proposed threshold is that it encourages suppliers to add new capacity quickly, far sooner than the time they would need to build new units. We do not believe that a 100 percent threshold provides the same benefit. Moreover, the Settling Parties negotiated and agreed on a threshold level as part of the overall Settlement Agreement, which was approved by a significant

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[122] ISO New England, Regional System Plan 2005 at ES-9.

majority of the NEPOOL Participants Committee. Given that we find that this provision creates appropriate incentives to bring on potentially cheaper capacity more rapidly, we will accept the 20 percent/40 megawatt provision.

140. New import capacity is capacity that a party without a multi-year contract wishes to bid into the FCA; it will be required to meet the financial assurance as well as physical backing requirements described above. This provision is intended to increase the level of eligible capacity in instances where new capacity is required to meet reliability criteria. Allowing additional imports to bid into the FCM, provided eligibility requirements are met, is reasonable as this increases the supply of capacity available in the auction.

e. Capacity Transfer Rights

141. NSTAR states that the settlement continues a discriminatory allocation of Capacity Transfer Rights (CTR) to municipal entities at the expense of investor-owned utilities. NSTAR states that Pool Planned Units (PPUs) should not be singled out in this manner because they do not support the transmission system at any greater level than other customers. NSTAR states that without this CTR allocation, owners of PPUs will continue to receive their entitlements in the PPUs. NSTAR states that if the Commission allocates CTRs to the municipals, then the investor-owned utilities should be allocated CTRs based on their interest in PPUs at the time they were divested.

142. Reading supports the settlement and states that the right to self-supply by load serving entities is a critical component for vertically integrated utilities such as itself. Reading states that its investment in PPUs and associated transmission upgrades was made prior to the

creation of the ISO and were based on the PPUs being fully integrated with load throughout the region. Referencing prior Commission orders that recognize the nature of the pre-existing contracts, Reading states that these life-of-unit contracts are specific entitlements by which they meet their energy and capacity obligations. Reading also states that the Presiding Judge, in the Initial Decision, ruled that the PPU Entitlement holders be allocated CTRs.[123]

143. MMWEC and Reading submit that were the Commission to modify the Settlement as requested by NSTAR, they would oppose the Settlement. They state that the PPU/CTR provisions contained in the Settlement counterbalance other financial burdens placed on consumers.

Commission Conclusion

144. The Commission will not alter the contractual arrangements relating to the PPUs. Municipal utilities have invested in these assets under a prior standard providing that their output would be fully available to the utilities. The municipals continue to be the original holders of these life-of-units contracts that are an important part of their ability to meet energy needs and to self supply capacity to meet pool obligations from their own resources. The Presiding Judge found in the Initial Decision that this differentiated the municipal entities that remain vertically integrated from utilities such as NSTAR who have divested themselves of these entitlements; and, therefore, found that subsequent holders of these entitlements no longer have the same obligations as the original owners.[124] We agree with this finding and also find that the proposed Settlement Agreement con-

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[123] *See* Initial Decision at P 703.

[124] Initial Decision at P 704.

tinues to preserve these arrangements consistent with past Commission policy. In its June 28, 2000 Order addressing the proposals to implement a congestion management and multi-settlement system in New England, the Commission recognized these entitlements and awarded Auction Revenue Rights to the entitlement holders to allow them to import the output into the congested NEMA zone for the life of their contracts, noting the circumstances of these pre-existing contracts.[125] We find that NSTAR has provided no basis that CTRs should be awarded to entities that no longer own these contracts and our June 2000 Order does not contemplate continuation of these rights for contracts that are no longer held.

f. Market Monitor Review of Exports

145. According to LIPA, under section III.D.4 of the Settlement Agreement, the Market Monitor will automatically review export bids by de-listed capacity. LIPA objects to this automatic review unless there is an indication of an exercise of market power. LIPA states that the "automatic review provision . . . assumes . . . an attempt to exercise market power" and that this provision is a discriminatory and unjustified disruption of market transactions.[126] LIPA states that the market rules in this regard should specify criteria that the Market Monitor will apply. LIPA also states that the settlement does not specify the types of actions that the Market Monitor may take regarding export transactions and urges the Commission to modify the settlement to require that conduct and impact criteria be used to trigger action by the Market Monitor and that these criteria be included in the market rules.

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[125] *See ISO New England, Inc.*, 91 FERC ¶ 61,311 at 62,073 (2000).

[126] Comments of LIPA at 8.

146. ISO-NE replies that LIPA has not set forth credible reasons why certain de-listed capacity is entitled to an exemption from independent Market Monitor review. Load Supporters reply that contrary to LIPA's assertion, the Market Monitor only reviews export bids greater than 0.8 CONE and that this provision provides a reasonable threshold for identifying bids that may warrant review while avoiding an undue burden on market participants.

Commission Conclusion

147. We will not modify the settlement's provisions regarding Market Monitor review of export bids. An export bid has a similar effect on the capacity market as a bid to de-list, since both bids remove capacity from New England loads. While a bid to export all of a suppliers' capacity may not be the exercise of market power (since the seller would not benefit from any increases in prices within New England), a bid to export capacity in tandem with a bid to sell capacity in New England could represent an exercise of market power. Therefore, we agree with ISO-NE that export bids should be reviewed by the Market Monitor in the same manner as de-list bids, to guard against the potential exercise of market power when an export bid is coupled with a bid in the capacity market. LIPA has not provided evidence as to why export transactions should be exempt from review by the Market Monitor and has not provided details as to how the settlement should be modified. Moreover, we will not require the alteration of the settlement in order to accommodate LIPA's concerns over market rules which have yet to be written, vetted through the stakeholder process, or filed with the Commission. The settlement does not represent the detailed market rules which will be filed later. As such, LIPA's concerns regarding the market rules are premature.

g. Assessment of Tie Line Capability

148. LIPA raises concerns regarding the ability of ISO-NE under the Settlement Agreement to impose limitations on capacity import and export transactions by assessing the capabilities of ties to adjoining control areas. Specifically, LIPA is concerned about tie benefits on its two interconnections with New England (the Cross Sound Cable and the 1385 cable) and argues that the FCM market rules should clarify tie benefits since LIPA's ties connect through a constrained region. LIPA requests that the Commission clarify that nothing in this settlement will set a precedent for the appropriate means by which ISO-NE will determine the tie benefits.

Commission Conclusion

149. LIPA has not provided evidence that this issue needs to be addressed here, and has not specified any specific provisions of the Settlement Agreement that give rise to its concerns. To the extent that this issue deals with market rules that have not been submitted to the Commission, it is premature to address this issue at this time.

h. Price Setting Mechanism

150. As discussed above, the FCM will not utilize a downward sloping demand curve like LICAP would have, instead employing a descending clock auction. PSEG states that, without a downward sloping demand curve, FCM will only procure that quantity of capacity sufficient to meet ISO-NE's projected installed capacity requirement. As a result, PSEG argues that the FCM will produce price volatility as well as volatility of reliability. PSEG asserts that only new units will be able to set prices significantly greater than zero and that such bids will be accepted only when shortage conditions are already present or imminent. PSEG contends that the

FCM will produce capacity prices at or near zero until shortages occur. When shortages occur, argues PSEG, prices will reach the CONE, perhaps for a single year, and then drop to zero again. PSEG appears to contend that, without a downward sloping demand curve as well as a mechanism to procure more than 100 percent of the installed capacity requirement, the FCM will not encourage the development and financing of new capacity resources. PSEG maintains that a demand curve mechanism like the LICAP model or PJM's Reliability Pricing Model (RPM) would provide the long-term price stability lacking in the Settlement Agreement.

Commission Conclusion

151. In this order we find that the Settlement Agreement is just and reasonable as a package and, therefore, we are not proposing modifications that would mandate the development of a demand curve in addition to the FCM. As the Commission recently stated in its order on PJM's proposed RPM mechanism, "there is not a single just and reasonable method for satisfying capacity obligations."[127] PSEG does not oppose the Settlement Agreement, and does not explain how the downward sloping demand curve should be integrated into the FCM.

i. Availability Metric/Compatibility With Adjoining Markets

152. As described above, the Settlement Agreement includes an availability metric that will reduce capacity payments to account for availability during designated periods of system stress (*i.e.*, Shortage Events). PSEG states that ISO-NE and capacity purchasers have argued that performance incentives assure that capacity re-

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[127] *PJM Interconnection, L.L.C.*, 115 FERC ¶ 61,079 at P.103 (2006).

sources are providing reliability benefits when the system needs them most. PSEG argues, however, that sufficient incentives already exist for generators to come online or to provide reserves during periods of peak demand. PSEG argues that generators will add a risk premium to capacity offers (to protect against outages) in response to the shortage events approach to measuring availability. PSEG argues that neither ISO-NE nor other proponents have demonstrated that the resulting higher costs to consumers justify enhanced system reliability.

153. PSEG and LIPA argue that the shortage events proposal redefines the nature of the capacity product. Both NYISO and PJM currently measure generator availability based on EFORd. PSEG and LIPA assert that adoption of the shortage events proposal would implement a capacity product that differs greatly from neighboring markets, and would create an undesirable seam between New York and New England. LIPA notes that during the transition, the value of capacity will be adjusted by the weighted EFORd availability metric which is not done in NYISO and PJM. LIPA asserts that the Initial Decision found that availability of generation in New England should continue to be applied and measured using the EFORd approach, based on Commission precedent and conformity with the NYISO and PJM. LIPA argues that the Commission should require ISO-NE to demonstrate that the use of this new standard of availability will be consistent with the EFORd measure. LIPA adds that modifications to the current capacity product should be left for broader regional discussions. PSEG asserts that PJM's RPM approach to resource adequacy provides a superior alternative to the FCM design, and the Settlement Agreement should not serve as a model for markets outside of New England. LIPA urges the Commission to ensure that the market rules,

when filed, are compatible with neighboring capacity markets and also urges the Commission to require that ISO-NE file an implementation report that details how external transactions will be integrated with FCM.

154. NYISO, in reply, requests that the Commission not take action that would require significant changes to the New York ICAP market but give full consideration to any unintended consequences of FCM on trade between the markets, and require an explanation and analysis of compatibility as the settlement is more fully developed.

155. In its answer, ISO-NE asserts that the interim EFORd proposal (for use during the transition period) and the FCM shortage events proposal are designed to ensure tradability across regions. ISO-NE states that during the interim period and thereafter, it will continue to calculate EFORd for all generating units in New England and thus trade between New York and New England will not be impeded. ISO-NE states that although capacity would be bought and sold in a way that is slightly different from the method used in New York, ISO-NE proposes to translate between these two different capacity products.

156. Load Supporters submit that the shortage event proposal provides more effective incentives for generators to supply resources to be responsive during stress periods than EFORd. Load Supporters also support the availability provisions that would expel underperforming units from the capacity markets, stating that the units will be replaced by better-performing resources. Load Supporters argue that the Settlement Agreement's availability metric does not create an insurmountable trade "seam." Load Supporters contend that the shortage event proposal satisfies the reliability and resource adequacy needs for New England load and that the EFORd metric that LIPA advocates does not. Capacity Sup-

pliers indicate that it accepts the "shortage events" methodology as part of the settlement package.

Commission Conclusion

157. ISO-NE's LICAP proposal contained an approach to measuring a generator's availability that differs from the conventional EFORd method. EFORd calculates "average availability over all hours of the year."[128] A generator's EFORd score is reduced only for forced outages.[129] In the LICAP proceeding, ISO-NE's proposed method for measuring a generator's availability was based on "shortage hours," which were hours in which ISO-NE was short of operating reserves, rather than EFORd. There, ISO-NE argued, EFORd would treat a generator outage during a cool spring afternoon the same as an outage during the hottest day of the summer, and would send a price signal that power is worth the same whether the level of demand is very high or very low.

158. Many of the parties representing load supported ISO-NE's shortage hours proposal. This element of the LICAP proposal was contested vigorously in the LICAP hearing and subsequent briefs. The Initial Decision stated that while ISO-NE had successfully shown that EFORd was "not perfect and that the Shortage Hours approach may provide a better overall availability metric," ISO-NE had not successfully shown that the EFORd approach is so imperfect as to be unjust and unreasonable.[130] In the Initial Decision, the Presiding Judge concurred with the Capacity Suppliers and other suppliers that it was not an opportune time to replace EFORd with a new metric. However, the Presiding Judge stated

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[128] Brief on Exceptions of ISO-NE at 9.

[129] *Id.*

[130] Initial Decision at P 546.

that the revised availability metric held promise and emphasized that "availability should continue to be defined using the EFORd metric *at this time*."[131] The Commission also provided an opportunity for ISO-NE to further develop its shortage hours approach, directing ISO-NE to file that proposal in a compliance filing.[132]

159. The Commission will accept the shortage events method proposed in the Settlement Agreement. We find that it is a more appropriate measure of availability, and provides an appropriate incentive for generators to provide reliable service during the periods of system stress, which preserves reliable service. The evidence offered in the hearing and in post-hearing briefs suggests that the current EFORd measurement (as contrasted to the modified measurement proposed for the transition period) may not appropriately measure the availability of capacity resources during times when they are most needed, and therefore deserving of full compensation for the service they provide. The Commission believes that it is reasonable for market participants to elect to measure availability in a manner that emphasizes hours of high demand. Moreover, the Commission believes that achieving resolution in the settlement discussions would have been very difficult without a revised measurement tool for availability; modifying the shortage event mechanism at the request of PSEG and LIPA, neither of which formally oppose the Settlement Agreement, would be unreasonable.

160. With regard to transactions with neighboring markets, ISO-NE states that it will continue to calculate EFORd for all generating units in New England during the transition period and thereafter. We find that this

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[131] *Id.* at P 548 (emphasis in the original).

[132] *Devon Power LLC*, 113 FERC ¶ 61,075 (2005).

will adequately address LIPA's and PSEG's concerns and will continue to allow exports and imports of capacity between ISO-NE and neighboring markets.

j. Relationship to RMR Agreements

161. Objecting Parties argue that the Settlement Agreement is defective in that 1) it does not immediately terminate existing RMR agreements and 2) does not prohibit the filing of new RMR agreements for several years. Objecting Parties argue that the Settlement Agreement should provide for a re-determination of RMR eligibility in light of the transition payments. Objecting Parties assert that the transition payments are so large that many, if not all, entities now charging RMR rates would be ineligible for those rates.

162. Objecting Parties submit that the locational forward reserves market, which is to be implemented in fall 2006, is devoted to compensating seldom-run resources that are needed for contingency support, particularly in congested areas.[133] Objecting Parties believe that the locational forward reserves markets and other market revisions should render an installed capacity market superfluous. Thus, Objecting Parties argue, all RMR contracts that have been granted since the April 25 Order should terminate on the first day of the locational forward reserves market. Objecting Parties argue that the Commission should modify the transitional provisions of the Settlement Agreement to provide for the termination of all Commission-approved RMR contracts. Objecting Parties argue that, after termination of the RMR agreements, holders would be permitted to reapply for new

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[133] The locational forward reserves market (LFRM), was proposed to the Commission in a filing on February 6, 2006 (Docket No. ER06-613-000) and approved in a Commission order issued May 12, 2006. *ISO New England, Inc.*, 115 FERC 61,175 (2006).

agreements only upon a showing that, even with interim payments, their receipts would be less than going-forward costs and make clear that any future RMRs would be limited to going-forward costs.

163. PSEG argues that the FCM design will not reduce the need for RMR contracts and may encourage the use of RMR contracts. PSEG argues that existing generation that is unable to set clearing prices may have to retire; where that generation is required for reliability, the only alternative would be to seek an RMR contract. PSEG also argues that the shortage event proposal will impose greater risks on older units that may be needed to maintain reliability. PSEG contends that, as such, the proposed FCM design encourages the retirement of these older units, and RMR agreements will be necessary to retain them. PSEG believes that PJM's RPM proposal provides a superior alternative and should serve as the model for future capacity markets.

164. Milford Power argues that Objecting Parties' arguments regarding RMRs contain several impermissible collateral attacks on prior Commission orders. Milford Power and ISO-NE argue that, with regard to termination, the Commission has ruled in several proceedings that RMR agreements should terminate only upon the implementation of a locational capacity mechanism. ISO-NE argues that a party may file a section 206 complaint to terminate any RMR agreement based on changed circumstances (*e.g.* demonstration that there is no longer a financial need). ISO-NE also notes that the Settlement Agreement states that nothing therein "prejudices the rights of any party to challenge, seek to terminate or support an RMR agreement on any other ground or restrict any party's rights to seek, agree to, or oppose any RMR

modifications."[134] Concerning limiting RMRs to going forward costs, Milford Power argues that the Commission has repeatedly ruled that an eligible RMR unit is entitled to recover its full cost of service.

165. ISO-NE submits that locational forward reserves market revenues only go to approximately 2,000 to 3,000 megawatts of generation out of a total of 32,000 megawatts of generation. ISO-NE states that while the locational forward reserves markets is an important market enhancement, it is only a partial remedy for revenues that need to be restored through a capacity market. Berkshire Power states that the Settlement Agreement recognizes that the fixed transition payments will not be adequate to compensate ICAP resources operating under an RMR agreement. CMEEC and MMWEC disagree and argue that the Commission should reject any such interpretation. CMEEC and MMWEC argue that the Settlement Agreement does not recognize anything with respect to the adequacy of transition payment revenues to compensate any or all RMR resources, or that the termination of existing RMR agreements cannot be sought for any legitimate reason.

Commission Conclusion

166. The Commission will not require the termination of existing RMR agreements prior to the full implementation of the FCM and will not require RMR holders to reapply for new RMR agreements. The Commission has consistently accepted RMR agreements for a term that expires upon implementation of a locational capacity mechanism.[135] FCM will not result in the purchase of ca-

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[134] Settlement Agreement at VIII.F.

[135] *See, e.g., Devon Power LLC*, 106 FERC ¶ 61,264 (2004) (*Devon Power*); *Mirant Kendall, LLC and Mirant Americas Energy Marketing, L.P.*, 109 FERC ¶ 61,227 (2004), *order on reh'g*, 110 FERC

pacity until the beginning of the first commitment period in June 2010. Therefore, the June 2010 termination date of RMR agreements is consistent with the express terms of the RMR agreements and the Commission's intent that those contracts terminate when a capacity market mechanism is fully implemented.[136] The Commission notes that the transition payments will be netted against RMR revenues, which will protect against over-recovery. Furthermore, the Settlement Agreement explicitly states that participants do not waive their rights to challenge the need for RMR contracts, given changes in a generator's compensation or changes to system infrastructure.[137]

167. Objecting Parties' arguments regarding the forward reserves market are misplaced in this proceeding, and accordingly, we reject them. This proceeding focuses solely on the capacity market, and the Commission has already ruled on issues related to the implementation of the forward reserves market.[138] As the Commission noted in its order approving the implementation of that market,

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¶ 61,272 (2005) ; *PSEG Power Connecticut, LLC*, 110 FERC ¶ 61,020, *order on reh'g*, 111 FERC ¶ 61,441, *order on reh'g*, 111 FERC ¶ 63,023 (2005); *Milford Power Company*, 110 FERC ¶ 61,299, *order on reh'g*, 112 FERC ¶ 61,154 (2005); *Bridgeport Energy, LLC*, 112 FERC ¶ 61,077, *order on reh'g*, 113 FERC ¶ 61,311 (2005), *reh'g rejected*, 114 FERC ¶ 61,265 (2006); *Berkshire Power Company, LLC*, 112 FERC ¶ 61,253 (2005), *reh'g denied*, 114 FERC ¶ 61,099 (2006), *reh'g rejected*, 115 FERC ¶ 61,253 (2006); *Consolidated Edison Energy Massachusetts, Inc.*, 112 FERC ¶ 61,263 (2005); *reh'g pending*; *Pittsfield Generating Company, L.P.*, 115 FERC ¶ 61,059 (2006), *reh'g pending*.

[136] *See Id.*

[137] *See* Settlement Agreement at section XIII.F.

[138] *New England Power Pool and ISO New England, Inc.*, 115 FERC ¶ 61,175 (2006).

"markets for capacity and operating reserves are separate, distinct and non-duplicative."[139]

168. The Commission disagrees with the comments made by PSEG regarding the potential for the FCM to induce additional RMR agreements. While existing units may not be able to set the clearing price in all auctions, they will receive revenues from the capacity market that, combined with other revenues, will provide them more of an opportunity to recover their costs than the current "all or nothing" capacity market. Moreover, PSEG voted not to oppose the Settlement Agreement and "[does] not request any specific modifications thereto."[140] PSEG's statement that PJM's RPM proposal provides a superior alternative suggests that it is using this proceeding to indicate its support for PJM's RPM proposal. This is not the appropriate forum.

169. With regard to Berkshire Power's comments, the Commission agrees with CMEEC and MMWEC: there is nothing in the Settlement Agreement that explicitly states that fixed transition payments will not be adequate to compensate ICAP resources operating under RMR agreements. Again, if this change in circumstances warrants termination of an RMR agreement, parties retain their rights to challenge the continued need for the contract.

k. Implementation of Scarcity Pricing

170. PPL believes that the FCM (and the transition period) alone will not be effective in solving New England's long-term reliability problems. PPL recommends that ISO-NE be required to install enhanced scarcity pricing in the energy market in addition to the FCM proposal.

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[139] *Id.* at P 78.

[140] Comments of PSEG at 1.

PPL argues that scarcity pricing would permit prices to reflect the value of energy based on supply and demand conditions, increase the amount of price responsive demand, and provide incentives for long-term contracts and generation construction (in both peaking and baseload facilities). PPL believes that the FCM model is compatible with enhanced scarcity pricing in the energy market. Maine Parties contend that PPL's request is beyond the scope of the proceeding and that the proper approach for seeking market changes is through the stakeholder process and/or a filing pursuant to section 206 of the FPA.

Commission Conclusion

171. The Commission agrees with Maine Parties that these arguments are beyond the scope of this proceeding. We encourage PPL to pursue its interests within the stakeholder process.

3. **Other Issues**

a. **"Public Interest" Standard of Review for Prices and Modifications**

172. Section 4.C of the Settlement Agreement states:

> From the Effective Date, absent the agreement of all Settling Parties to the proposed change, the standard of review for: (i) challenges to the Capacity Clearing Prices derived through the FCA and prices resulting from reconfiguration auctions provided for in the Settlement Agreement and in the Market Rules addressing the terms of the Settlement Agreement that are approved or accepted by the FERC pursuant to section 3, and (ii) proposed changes to section 11, Part VIII below (Agreements Regarding Transition Period) and the Market Rules implementing that part, shall be the "public

> interest" standard of review set forth in *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332 (1956) and *Federal Power Commission v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956) (the "Mobile-Sierra" doctrine), whether the change is proposed by a Settling Party, a non-Settling Party, or the FERC acting *sua sponte*. This Settlement Agreement does not impose the Mobile-Sierra standard on any provision of this Settlement Agreement or the Market Rules that address the terms of the Settlement Agreement except as expressly provided in this section 4.C.

173. IECG opposes this provision, arguing that it represents an attempt by the settling parties "to write a broad exception to the statutory provisions of the FPA, not only for themselves . . . but also as a broad disenfranchisement of non-Parties from the protections against unjust and unreasonable rates provided in the FPA."[141] Additionally, it argues that this provision improperly amends the NEPOOL Participants Agreement by restricting the authority of ISO-NE to protect customers except in the case of exigent circumstances (pursuant to section 11.2 of the Participants Agreement). Accordingly, IECG argues, acceptance of this provision by the Commission would lead to imprudent and unlawful results.

174. More specifically, IECG asserts that as a policy matter, the Commission is not bound to follow any particular methodology when setting rates as long as the resulting rate is just and reasonable. Section 4.C of the Settlement Agreement would alter this regulatory paradigm, IECG contends, by adopting a particular rate methodology in advance of the actual results of the as-yet

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[141] Comments of IECG at 16.

untested market mechanism. It further argues that the New England RTO Governance Process and the Commission's continued authority to assure the justness and reasonableness of rates address any fears of uncertainty that this settlement provision may be intended to resolve. Furthermore, IECG suggests that tying the hands of ISO-NE, NEPOOL and the Commission to respond to unexpected developments of a matter of such importance may encourage market participants to search for and seek to benefit from design flaws.

175. Additionally, IECG states that section 4.C of the Settlement Agreement would unlawfully amend the Participants Agreement and Regional Transmission Organization (RTO) governance procedures that specifically allow participants to make proposals for changes to the market rules (and have those proposals considered in the NEPOOL Committee process and, with support, by the Commission), and entitle participants to the faithful and independent execution by ISO-NE of its duties.[142] According to IECG, these procedures explicitly do not permit market rules or procedures to be adopted outside of the NEPOOL advisory framework. IECG argues that ISO-NE and NEPOOL may not abrogate the procedural rights of market participants under the governing framework to make proposals for changes to the market rules through the insulation of particular market rules under a settlement. Further, IECG notes that section 17 of the Participants Agreement sets forth a process for amending the rights of parties under that agreement that was not observed. IECG maintains that accepting a waiver of this process through the joining of a settlement by ISO-NE or NEPOOL would invite a dismantling of

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[142] *See Id.* at 18-19, *citing* section 11 of the NEPOOL Participants Agreement.

the carefully balanced governance structure in New England.

176. Last, IECG asserts that section 4.C attempts to revoke the section 206 protections given to non-parties, and notes that the Commission has rejected such attempts in the past.[143] Even if the Settlement Agreement could be characterized as a contract, IECG argues, the parties have no legal ability to revoke the statutory protections of section 206. According to IECG, in analogous circumstances the Commission has rejected an attempt by the signatories to an agreement to limit the ability of non-parties to file challenges under section 206.[144]

177. In reply, several parties note that this provision only applies the *Mobile-Sierra* public interest standard to limited provisions of the Settlement Agreement, namely (i) challenges to the clearing prices in the FCA and any reconfiguration auctions provided for in the market rules adopted pursuant to the Settlement Agreement, and (ii) proposed changes to the provisions of the settlement regarding the transition period and the market rules implementing those provisions. Capacity Suppliers argue that it is not unusual for parties to a settlement to use *Mobile-Sierra* to provide greater price certainty, which will in turn provide lower prices for consumers. ISO-NE agrees, arguing that use of the *Mobile-Sierra* provision in this instance will reduce regulatory uncertainty and the risk premium that may be required by new entrants. According to Capacity Suppliers, the market would suffer if the final auction clearing process were in

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[143] Comments of IECG at 21-22, *citing Carolina Power & Light Company and North Carolina Electric Membership Corporation*, 67 FERC ¶ 61,074 (1994) and *Northeast Utilities Service Corporation*, 66 FERC ¶ 61,332 (1994).

[144] Comments of IECG at 22, *citing PJM Interconnection LLC*, 96 FERC ¶ 61,206 (2001).

jeopardy each time a consumer thought prices were too high or a seller thought prices were too low. Similarly, NEPOOL states that this provision was intentionally limited and crafted with the narrow purpose of providing certainty during the transition period and price certainty and finality to the auction prices.[145]

178. Further, Capacity Suppliers note that the *Mobile-Sierra* provision will not remove the risk of legal challenges, and the Commission cannot cede its authority under the FPA to ensure just and reasonable rates. Nevertheless, Capacity Suppliers contend, the Supreme Court allows parties to agree (via a *Mobile-Sierra* clause) that a stronger showing must be made before contract rates can be changed. Additionally, it argues that "[t]here is . . . 'no Commission or court precedent that supports a finding that a non-signatory [such as IECG] may unilaterally seek changes to a *Mobile-Sierra* 'public-interest' contract under the 'just and reasonable' standard of review.'"[146] Similarly, NEPOOL states that contrary to IECG's arguments, the Commission has consistently approved the use of the *Mobile-Sierra* standard for rates and terms established under a settlement agreement, and has consistently held that *Mobile-Sierra* protection does not

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[145] NEPOOL states that this provision is far more limited than that standard that would be applied under the Commission's Notice of Proposed Rulemaking in Docket No. RM05-35-000. *See Standard of Review for Modifications to Jurisdictional Agreements*, 71 Fed. Reg. 303, FERC Stats. & Regs. ¶ 32,596 (2006). According to NEPOOL, if adopted, under those regulations *Mobile-Sierra* protections would serve as a default for review by the Commission of jurisdictional agreements (including settlement agreements) that are not signed by all signatories and are otherwise silent regarding the standard of review.

[146] Reply Comments of Capacity Suppliers at 32, *citing Midwest Independent Transmission System Operator, Inc.*, 110 FERC ¶ 61,380 at P 24 (2005).

"unjustly deprive a non-settling party from statutory rights to seek revisions to the terms or conditions of a filed settlement agreement."[147] American National Power also argues that section 4.C is fully consistent with recent Commission policy, noting that the Commission has on several occasions approved similar *Mobile-Sierra* provisions applying the public interest standard of review for both signatories and non-parties.[148] As a result, American National Power states that there is no justification for deleting the provision from the settlement, particularly where doing so would threaten to undo the efforts of the parties to achieve a broadly-supported settlement.

179. Capacity Suppliers and ISO-NE also explain that the Settlement Agreement contains several provisions permitting challenges to the auction prices before they become final. First, they note that section 3.B of the settlement permits parties to challenge the market rules that are filed with the Commission to the extent that they are inconsistent with the settlement. Second, under Part IX of the Settlement Agreement, ISO-NE must make an informational filing with the Commission 90 days before an FCA runs, specifying any separate zones that will be employed, the bids that qualify for participation in the market, and the Market Monitor's conclusions regarding the acceptability of bids in the auction. Interested parties have 15 days to file comments on this filing, and the Commission may order changes to the planned auction within 75 days. Finally, Capacity Suppliers and ISO-NE state that section 11 of Part II.G.3.b requires ISO-NE to file the results from the primary auctions under section 205 of the FPA, and parties will have 45 days to file objections to those auction results. Thus, they contend,

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[147] Reply Comments of NEPOOL at 17-18 (citations omitted).

[148] Reply Comments of American National Power at 15-16 (citations omitted).

the Settlement Agreement provides parties with "extraordinary protection" to voice their concerns regarding the justness and reasonableness of the auction prices while appropriately balancing a need for price certainty by giving the auction prices *Mobile-Sierra* protection once final.[149]

180. Capacity Suppliers also assert that IECG does not raise any specific argument as to why the transition provisions should not be afforded *Mobile-Sierra* protection. It argues that IECG and others are already challenging these provisions under the just and reasonable standard through their settlement comments, and thus should not be afforded another opportunity to challenge those provisions at a later date.

181. NEPOOL asserts that IECG has misconstrued the impact on the stakeholder process of the limited *Mobile-Sierra* protections in the Settlement Agreement. Rather than "paralyzing" the stakeholder process as IECG contends, NEPOOL argues that the settlement specifically calls for the development of market rules within the stakeholder process in the NEPOOL Participants Agreement and through consultation with state agencies. Under this framework, ISO-NE retains its independent judgment and participants may support alternative market rules if support exists among the stakeholders. IECG and all other market participants, NEPOOL contends, are not limited by the *Mobile-Sierra* provision in their ability to vote in support of or in opposition to the market rules that are developed under the Settlement Agreement. Finally, NEPOOL argues that nothing in the NEPOOL Participants Agreement prohibits ISO-NE or NEPOOL from agreeing to a *Mobile-Sierra* provision

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[149] Reply Comments of Capacity Suppliers at 33; Reply Comments of ISO-NE at 53.

in a settlement agreement, and that such a limitation on NEPOOL's ability to settle contested matters would be ill advised.

Commission Conclusion

182. IECG appears to interpret section 4.C more broadly than it is intended to apply. Our reading of the provision indicates that, as several reply commenters note, the "public interest" standard will only apply to (1) the final clearing prices in the FCA and any reconfiguration auctions permitted under the market rules, and (2) the transition mechanism. The *Mobile-Sierra* provision does not apply to the market rules that will be developed and filed with the Commission under the Settlement Agreement or to any other aspect of the settlement not specifically mentioned in section 4.C. Therefore, IECG's concerns that the *Mobile-Sierra* clause will broadly eliminate the ability of parties to exercise their rights under the FPA are misplaced.

183. The Commission will not require the Settling Parties to revise the limited *Mobile-Sierra* provision included in the Settlement Agreement. As NEPOOL, Capacity Suppliers and American National Power correctly state, the Commission has routinely permitted the use of similar provisions in settlement agreements, including contested settlements.[150] Moreover, as the Com-

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[150] *See, e.g., Midwest Independent System Operator, Inc.*, 115 FERC ¶ 61,174 (2006); *Midwest Independent System Operator, Inc.*, 110 FERC ¶ 61,177 (2005); *Midwest Independent System Operator, Inc.*, 110 FERC ¶ 61,380 (2005); *Pennsylvania-New Jersey-Maryland Interconnection*, 105 FERC 61,294 (2003), *reh'g denied*, 108 FERC ¶ 61,032 (2004); *Vermont Electric Cooperative, Inc.*, 114 F.E.R.C. ¶ 61,220 (2006); *Calpine Construction Finance Company, L.P.*, 114 F.E.R.C. ¶ 61,217 (2006); *Hermiston Power Partnership*, 114 F.E.R.C. ¶ 61,204 (2006); *Central Maine Power Company*, 114 F.E.R.C. ¶ 61,184 (2006); *San Diego Gas & Electric Company*, 114

mission has stated on several recent occasions, "there is no Commission or court precedent that supports a finding that a non-signatory may unilaterally seek changes to a *Mobile-Sierra* 'public interest' contract under the 'just and reasonable' standard of review."[151] Therefore, as an initial matter, we conclude that the *Mobile-Sierra* provision is fully consistent with current Commission policy.

184. Furthermore, we find this *Mobile-Sierra* provision reasonable because it does not operate to the detriment of the parties who have not signed on to the Settlement Agreement. Those parties are still protected in several ways. First, as the court explained in *Northeast Utilities I*, "the most attractive case for affording additional protection ... is where the protection is intended to safeguard the interests of third parties."[152] The court noted there that "[t]he Mobile-Sierra doctrine itself allows for intervention by FERC where it is shown that the interests of third parties are threatened," noting that the standard articulated by the Supreme Court in such cases "is the protection of outside parties from 'undue discrimination' or imposition of an 'excessive burden.'"[153] Addi-

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F.E.R.C. ¶ 61,158 (2006); *Wisconsin Power & Light Co.*, 106 FERC ¶ 61,112 (2004).

[151] *Pennsylvania-New Jersey-Maryland Interconnection*, 108 FERC ¶ 61,032 at P 7, *citing Public Utilities Commission of the State of California*, 105 FERC ¶ 61,182 at P 50 (2003).

[152] *Id.*

[153] *Id.*, *citing United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332, 344-45 (1956) (*Mobile*) and *FPC v. Sierra Pacific Power Co.*, 350 U.S. 348, 355 (1956) (*Sierra*). *See also Papago Tribal Utility Authority v. FERC*, 723 F.2d 950, 953 n.4 (D.C. Cir. 1983) (*Papago*) (recognizing that the Commission's ability under the *Mobile-Sierra* doctrine to address undue discrimination under section 206 of the FPA includes the ability to address rates, terms and conditions of utility service that are "unduly discriminatory or pre-

tionally, in *Northeast Utilities II*, the court rejected the notion, expressed in Papago, that the public interest standard is "practically insurmountable."[154] Therefore, even under the "public interest" standard of review, the Commission retains significant authority to protect non-parties to the settlement from harm.

185. As several entities point out in the reply comments summarized above, the Settlement Agreement itself provides for thorough review of the final auction clearing prices. In particular, the Settlement Agreement provides that ISO-NE will make both an informational filing prior to the auction that includes information regarding the zones to be used and qualifying bids, and a section 205 filing following the auction containing the results. The limited *Mobile-Sierra* provision in section 4.C does not apply to these filings, and thus the Commission will review them under the just and reasonable standard. All parties will have the ability to comment on such filings, as set forth in the Settlement Agreement.

186. In conclusion, we believe that this limited *Mobile-Sierra* provision appropriately balances the need for rate stability and the interests of the diverse entities who will be subject to the FCM. Stability is particularly important in this case, which was initiated in part because of the unstable nature of ICAP revenues and the effect that has on generating units, particularly those who are critical to maintaining reliability. "The court has repeatedly emphasized the importance of contractual stability in a

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ferential to the detriment of purchasers who are not parties to the contract.").

[154] *Northeast Utilities Service Co. v. FERC*, 55 F.3d 686, 691 (D.C. Cir. 1995) (*Northeast Utilities II*), *citing Papago*, 723 F.2d at 954. The court "noted that neither Mobile nor Sierra stated or intimated that the 'public interest' doctrine was 'practically insurmountable.'" *Northeast Utilities II*, 55 F.3d at 691.

number of cases involving the *Mobile-Sierra* doctrine."[155] The Court's statement in *Mobile* that "all agree . . . [that] the stability of supply arrangements . . . is essential to the health of the natural gas industry" is no less true with regard to the health of New England's electricity infrastructure.[156] At the same time, we must ensure that rates for capacity meet our legal requirements. This limited *Mobile-Sierra* provision achieves that balance.

b. Due Process

187. Objecting Parties argue that opponents of LICAP have not been afforded due process. First, they note that ISO-NE, when it originally filed LICAP, committed to conduct a "regional dialogue," which began only with the recent settlement discussions. According to Objecting Parties, the settlement discussions only offered generators an attractive alternative (*i.e.*, the LICAP mechanism) to a negotiated settlement. Objecting Parties assert that the Presiding Judge during the hearing procedures should have been given the opportunity to consider alternatives to the LICAP mechanism. Following the oral argument, Objecting Parties continue, the Commission could have structured a fair and balanced settlement process. Instead, they contend that "the Commission offered a Hobson's Choice," structuring a settlement process that gave generators all the leverage when it stated in the October 21 Order that "if the parties cannot agree upon a workable alternative, the Commission will be prepared to move promptly to consider the existing record and the Initial Decision."[157] This process, they ar-

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[155] *Potomac Electric Power Co. v. FERC*, 210 F.3d 403, 409 (D.C. Cir. 2000) (citations omitted).

[156] *Mobile*, 350 U.S. at 344.

[157] Comments of Objecting Parties at 18, *citing* October 21 Order at P 10.

gue, "forced load to buy its way out of the LICAP mechanism."[158] To rectify this problem, Objecting Parties assert that the Commission should provide a fresh start, and give parties the opportunity to decide whether the FCM is appropriate, free of the threat that the Commission will implement LICAP.

188. In reply comments, Capacity Suppliers state that the Commission should reject these claims. First, Capacity Suppliers argue that the Commission did not issue a "settle or LICAP" ultimatum as Objecting Parties claim, but simply noted that it was prepared to act on the record and Initial Decision before it. Second, Capacity Suppliers assert that the level of support for the settlement among load parties,[159] and the fact that the settlement contains much of what load parties argued for at the oral argument, confirms load's equal or superior leverage.[160] Finally, Capacity Suppliers argue that Objecting Parties' claims that the Commission violated their due process rights by not considering alternatives are without merit. They note that the Commission rejected alternatives originally offered in response to the initial LICAP proposal, and subsequently "bent over backwards" to give load parties the opportunity to present their arguments by permitting oral argument and estab-

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[158] Comments of Objecting Parties at 18.

[159] NEPOOL, in its reply comments, also states that the support of Load Supporters for the settlement contradict Objecting Parties' claim of a lack of bargaining power.

[160] Reply Comments of Capacity Suppliers at 6 (noting that the settlement includes a forward capacity market with no demand curve and an availability metric, which load parties argued for at the oral argument).

lishing additional settlement procedures at the request of load representatives.[161]

189. Similarly, ISO-NE states that NSTAR (one of the Objecting Parties) and others, in an October 7, 2005 letter to Chairman Kelliher, supported the institution of the settlement procedures they now protest as unbalanced, and did not indicate at the oral argument that a settlement procedure would be biased or unworkable. Further, it notes that the Connecticut and Massachusetts Attorneys General (also members of the Objecting Parties) supported the procedural proposal filed by CMEEC and MMWEC prior to the oral argument, which included a settlement process mediated by a Commission Administrative Law Judge of the parties' choosing that would conclude on February 1, 2006. Moreover, ISO-NE notes that load representatives achieved almost unanimous political consensus that LICAP should not be adopted, and their efforts resulted in a provision in the Energy Policy Act of 2005 urging the Commission to carefully consider the states' objections. These actions do not evidence a lack of bargaining power or leverage, ISO-NE argues. Additionally, ISO-NE contends that the fact that almost all of the elements of the market design advocated by NSTAR and the Energy Consortium prior to and at the oral argument were adopted in the Settlement Agreement, and that the Objecting Parties do not quarrel with the overall design of the FCM, shows that their arguments are "a strategy of delay."[162] Finally, ISO-NE asserts that claims that LICAP opponents were not given an opportunity to present alternatives are now moot,

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[161] *Id.* at 6-7. Capacity Suppliers note that no load parties opposed the proposal to establish settlement procedures or sought rehearing of the procedures set forth in the October 21 Order.

[162] Reply Comments of ISO-NE at 24. *See also* Reply Comments of NEPOOL at 11.

since an alternative was adopted through the settlement procedures.

Commission Conclusion

190. "[C]onstitutional due process requires that a party affected by a governmental action be given 'the opportunity to be heard at a meaningful time and in a meaningful manner.'"[163] We agree with Capacity Suppliers and ISO-NE that this standard was more than satisfied in this proceeding. Through the course of this proceeding, parties have been given numerous opportunities to present evidence and lodge their objections to the various proposals for dealing with the deficiencies identified in the ICAP market. As recounted in the background and procedural history of this order, the Commission: (1) addressed requests for rehearing of the April 25 Order initially establishing these section 206 proceedings; (2) provided notice and opportunity for comment on ISO-NE's proposed LICAP mechanism, and addressed those comments in the June 2 Order setting portions of that proposal for hearing;[164] (3) established hearing procedures regarding specific critical aspects of the LICAP mechanism, giving all interested parties the opportunity to fully litigate those matters; (4) took the rare step of providing the parties with opportunity for oral argument before the Commission to present their arguments regarding the LICAP mechanism and to advance potential

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[163] *See City of Anaheim, California, City of Riverside, California*, Opinion No. 483, 113 FERC ¶ 61,091 at P 153 (2005) (*citing Mathews v. Eldridge*, 424 U.S. 319, 333 (1976)), *reh'g denied*, 114 FERC ¶ 61,311 (2006).

[164] As we noted in the March 23 Order I (in response to rehearing requests that the Commission might otherwise have rejected as untimely), the Commission considered alternatives to LICAP in the June 2 Order to the extent they were presented. March 23 Order I at P 18.

alternatives to the LICAP mechanism; (5) established settlement procedures to allow the parties an opportunity to develop an alternative to the LICAP mechanism; and (6) is now addressing comments regarding the Settlement Agreement. It is unclear to us what more process could have been provided consistent with constitutional principles, and Objecting Parties have not stated what additional procedures should have been provided, instead simply seeking to have the Commission abandon the Settlement Agreement and provide a "fresh start."

191. Moreover, Objecting Parties' misread the October 21 Order as establishing a "settle or LICAP" ultimatum. That order merely recognized that in light of the need for the Commission to address the status quo (which the parties to this case agree is failing), its only option outside of a settlement agreement providing an alternative to LICAP was to consider the extensive existing record in the case. The Commission did not suggest what action it would take regarding the Initial Decision. It simply acknowledged that review of the record and the Initial Decision was the next procedural step available if settlement talks failed. Finally, the Commission did not "structure" the settlement procedures at all, but simply provided the parties with additional time and the assistance of a Commission-appointed settlement judge (who was requested by the parties) to help the parties reach agreement on an alternative. This procedure did not give any party leverage in the settlement discussions.

c. Commission Jurisdiction over the Proposed Settlement Agreement

192. Objecting Parties argue that the Commission lacks jurisdiction to approve the Settlement Agreement. First, they note that section 202(a) of the FPA[165] encourages

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[165] 16 U.S.C. § 824a(a) (2000).

voluntary formation of power pools and grants the Commission jurisdiction over such pools, including the reserve sharing mechanisms proposed by pool members. Nevertheless, Objecting Parties contend, section 202(a) does not trump the limits on the Commission's jurisdiction in section 201 of the FPA, which leaves to the states "plenary authority over generation, including the determination of how much generation individual utilities must own or control to reliably serve retail customers."[166]

193. According to Objecting Parties, installed capacity has nothing to do with wholesale transmission of electric energy and is only tangentially related to wholesale sales of electricity. Objecting Parties note that the Commission has previously acknowledged, in both Order No. 888[167] and its orders in this proceeding, that matters related to the assessment of reliability and "resource adequacy" (or the amount of capacity necessary to serve loads) are within the interest and authority of the states.[168] Objecting Parties state that the Commission has previously respected this jurisdictional divide, under which power pool members are responsible for proposing

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[166] Comments in Opposition to Settlement of Objecting Parties at 26, *citing* 16 U.S.C. § 824a (2000).

[167] *Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, Order No. 888, 61 FR 21540 (May 10, 1996), FERC Stats. & Regs. ¶ 31,036 at 31,682 (1996), *order on reh'g*, Order No. 888-A, 62 FR 12274 (March 14, 1997), FERC Stats & Regs. ¶ 31,048 (1997), *order on reh'g*, Order No. 888-B, 81 FERC ¶ 61,248 (1997), *order on reh'g*, Order No. 888-C, 82 FERC ¶ 61,046 (1998), *aff'd in relevant part sub nom. Transmission Access Policy Study Group v. FERC*, 225 F.3d 667 (D.C. Cir. 2000), *aff'd sub nom. New York v. FERC*, 535 U.S. 1 (2002).

[168] Comments in Opposition to Settlement of Objecting Parties at 26-27.

and determining the justness and reasonableness of methods to share reserves.

194. Here, however, Objecting Parties state that the Commission has overreached the boundaries of its jurisdiction by directing ISO-NE to develop a new reserve sharing mechanism and has violated the limits of its jurisdiction in three respects. First, they contend that the Commission did not find the existing capacity market unjust and unreasonable, finding only that RMR agreements were distorting the wholesale market. According to Objecting Parties, the underlying cause of the increase in RMR agreements was a lack of local operating reserves in critical areas, which has been addressed by the locational forward reserves market. Moreover, Objecting Parties contend that the record does not show that all generators in NEPOOL need additional revenue through a revised capacity market or that all generators are earning insufficient revenues. Rather, they contend that the record shows that certain types of generators (coal and nuclear) are earning sufficient returns, making additional payments a windfall. Furthermore, they contend that the record shows that New England has a surplus of capacity, making it irrational to build new capacity (except in locally critical areas, which it argues the locational forward reserve market will address).

195. Second, Objecting Parties state that while RMR agreements are within the Commission's wholesale market jurisdiction, the Commission may not mandate minimum requirements for capacity and then dictate the prices for that capacity as a remedy for the proliferation of RMR agreements. Objecting Parties argue that the Commission oversteps it jurisdiction with regard to voluntary power pools by "mandating a scheme that is directed to determining how much generation needs to be available to meet local load requirements, and sets forth

the basis upon which owners of generation are to be compensated."[169] Moreover, Objecting Parties state that the Commission's lack of authority over the method by which a utility satisfies its reserve requirements requires that participation in any new capacity market construct must be voluntary.[170] Despite the provision in the Settlement Agreement permitting participants to self-supply capacity, they charge that the FCM "essentially requires [load serving entities] to meet their generation capacity reserve obligations through the FCM mechanism." Thus, Objecting Parties argue that if the Commission approved FCM, it would be imposing a resource adequacy requirement on New England utilities in contravention of the FPA.

196. Third, Objecting Parties argue that to the extent the current capacity market is flawed, ISO-NE may not make a proposal to correct those flaws because it is not a member of NEPOOL. They contend that directing ISO-NE to make a proposal amounts to a prohibited evisceration of the voluntary nature of power pools under section 202(a) of the FPA.

197. In reply comments, Capacity Suppliers respond that "the current ICAP market is without a doubt broken."[171] They note that the Commission has made several prior findings that the current capacity market is unjust and

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[169] *Id.* at 29.

[170] Objecting Parties also contend that states should be able to expressly opt out of the FCM and have their load serving entities be responsible for procuring capacity and reserves.

[171] *See* Reply Comments of Capacity Suppliers at 17, *citing* Oral Argument Tr. At 252:8-14 (Chairman Kelliher's closing remarks, noting that "[t]here does seem to be consensus around a threshold issue that there is a problem under the status quo that needs to be addressed.")

unreasonable.[172] Further, they contend that the record contains substantial evidence showing that existing resources are not recovering sufficient revenues, noting that even the evidence of those opposing LICAP showed that generators were recovering only 10 percent of what they would recover under the LICAP mechanism as approved by the Initial Decision.

198. Capacity Suppliers argue that the Commission has jurisdiction to approve the settlement, and that state regulators, having taken the steps to form a tight power pool and organized electricity markets, may not "pick and choose" which market design elements they will cede to Commission jurisdiction and which they will reserve to state jurisdiction. Capacity Suppliers assert that federal courts have confirmed the Commission's authority to allocate the costs of capacity among members of a power pool, even in the face of opposition from state regulators.[173] Capacity Suppliers contend that as the Commission has previously held in these proceedings, while the capacity market may impact state regulatory programs, the design of the capacity market itself is not within the jurisdiction of the states. Finally, they note that the Energy Policy Act of 2005 increases the Commission's jurisdiction over electric system reliability.

199. ISO-NE contends that Objecting Parties have ignored the Commission's prior determination on the issue of state jurisdiction over resource adequacy. In particular, ISO-NE argues that the Commission acknowledged

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[172] Reply Comments of Capacity Suppliers at 17-18.

[173] *Id.* at 40-41, *citing Mississippi Industries v. FERC*, 808 F.2d 1525, 1543 (D.C. Cir. 1987) (holding that the Commission had the authority to reallocate the costs of a nuclear generating facility among affiliated operating companies "pursuant to its exclusive rate authority over wholesale transactions and its remedial authority as set forth in sections 205 and 206" of the FPA.)

its jurisdiction over issues concerning the capacity market when it set the initial LICAP proposal for hearing, and has approved ISO-NE's authority to set installed capacity requirements, finding that doing so did not infringe on the state's resource adequacy jurisdiction.[174]

200. American National Power argues in reply that Objecting Parties' claims are an attempt to relitigate issues already decided by the Commission in these proceedings.[175] Additionally, American National Power argues that the Supreme Court has ruled "that the States cannot circumvent FERC's authority over the interstate transmission of electricity and wholesale electric sales by using their retail ratemaking authority."[176] It asserts that the issue in this proceeding is the price for wholesale capacity, which is clearly within the Commission's jurisdiction.

Commission Conclusion

201. The Commission has ample jurisdiction to consider and approve the Settlement Agreement. The settlement does not in any way alter the method by which resource adequacy requirements (particularly the installed capacity requirement) are determined or direct that a particular amount of capacity be installed, areas that the Commission has historically left to the states.[177] Also, as noted

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[174] Reply Comments of ISO-NE, *citing* June 1 2004 Order at P 58; *ISO New England, Inc.*, 111 FERC ¶ 61,185 at P 32 (2005).

[175] Reply Comments of American National Power at 19-20.

[176] *Id.* at 21, *citing Mississippi Power & Light Co. v. Mississippi ex rel. Moore*, 487 U.S. 354, 373 (1988).

[177] Currently, ISO-NE calculates capacity requirements to achieve "Objective Capability," or the total amount of capacity required by the system to meet peak load plus a reserve margin. Objective Capability is determined each year in accordance with Northeast

above, the Settlement Agreement contains provisions permitting load serving entities to self-supply their capacity obligations.[178] The Settlement Agreement and the tariff provisions that will follow it establish a mechanism and market structure for the purchase and sale of installed capacity at wholesale in interstate commerce and to determine the prices for those sales, bringing it squarely within the Commission's jurisdiction under the FPA.[179] Courts have confirmed that the Commission has jurisdiction under the FPA to regulate the charges for capacity in wholesale markets.[180] Objecting Parties do not point to any provision in the Settlement Agreement that establishes a resource adequacy requirement, or explain why the Commission does not have jurisdiction over the wholesale prices charged for the capacity product in New England. Objecting Parties' argument that load-serving entities are required to participate in the FCM (thus mandating participation in a resource adequacy program contrary to the FPA's limitations) fails because the provisions in the Settlement Agreement permit parties to self-supply their capacity obligations, and Object-

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Power Coordinating Council (NPCC) standards. *See* March 23 Order I at P 30.

[178] *See* Settlement Agreement, Part III.O.

[179] 16 U.S.C. § 824(b)(1) (2000) ("The provisions of this Part shall apply to the transmission of electric energy in interstate commerce and the sale of electric energy at wholesale in interstate commerce.")

[180] *See Municipalities of Groton v. FERC*, 587 F.2d 1296 (D.C. Cir. 1978) (holding that the Commission had jurisdiction over the installed capability charge in New England, a precursor to ICAP); *Mississippi Industries v. FERC*, 808 F.2d 1525 (D.C. Cir. 1987) (holding that the Commission could exercise jurisdiction over the allocation of the costs of capacity among four utility operating companies of a holding company under "its undisputed authority over the wholesale rates of electric generating facilities in interstate commerce.").

ing Parties have not explained why these provisions are insufficient.

202. Furthermore, the Commission fully addressed the issue of its jurisdiction in prior orders in this proceeding regarding the LICAP mechanism, and made clear that it did not intend to usurp the authority of the states' "central role in determining resource adequacy."[181] In its March 23 *Order on Rehearing and Clarification*, in particular, the Commission explained that the issue in this proceeding is not how the capacity requirement is calculated or how the responsibility for meeting that requirement is divided among load serving entities.[182] Instead, the issue is how prices for capacity are determined, to remedy identified flaws in the market.[183] As the Commission explained there, "the effect of this proceeding is not to impose a regional resource adequacy requirement, but merely to change the pricing."[184]

203. Objecting Parties are also incorrect in their assertion that the Commission did not find the existing capacity market unjust and unreasonable, as required by section 206 of the FPA. As the Commission explained in the June 2 Order, the April 25 Order directed revisions to the ISO-NE tariff "pursuant to section 206 of the [FPA]" to "implement . . . location or deliverability requirements in the ICAP or resource adequacy market . . . so that capacity within [designated congestion areas] may be appropriately compensated for reliability."[185] In the July 24 Order, the Commission further clarified that it was acting under section 206 of the FPA and formally stated

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[181] November 8 Order on Rehearing at 70.

[182] *Devon Power LLC*, 110 FERC ¶ 61,315 at P 29-32 (2005).

[183] *Id.*

[184] *Id.* at P 32.

[185] June 2 Order at P 29, *citing* April 25 Order at P 33, 37.

that it "found that Market Rule 1 created an unjust and unreasonable result" because RMR agreements, and the need for such agreements, caused an extensive disruption to wholesale markets.[186] Additionally, Objecting Parties' argument that the locational forward reserves market has addressed the underlying deficiencies in the capacity market is misplaced here, and is nonetheless unsupported by evidence.[187] To avoid any ambiguity, we reiterate here our prior finding that the existing ICAP market is unjust and unreasonable.

204. Further, we find without merit Objecting Parties' claim that the record does not show that generators are earning insufficient revenues. We agree with Capacity Suppliers that the record contains substantial evidence regarding the inability of generators to earn sufficient revenues in the current market, both to continue operating or to support new investment.[188] Moreover, as we have stated previously, the increase in RMR agreements in New England provides further substantial evidence that generators are failing to recover their costs and require additional revenues.[189]

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[186] June 2 Order at P 29, *citing* July 24 Order at P 33.

[187] Additionally, the Commission recently reiterated that "the markets for capacity and operating reserves are separate, distinct, and non-duplicative." *See New England Power Pool and ISO New England Inc.*, 115 FERC ¶ 61,175 at P 78 (2006); *see also New England Power Pool and ISO New England Inc.*, 105 FERC ¶ 61,204 at P 27 (2003).

[188] *See* Reply Comments of Capacity Suppliers at 18, *citing* Exh. ISO-23 (Rebuttal Testimony of David LaPlante in hearing); *see also supra* P 63.

[189] *See Devon Power LLC*, 110 FERC ¶ 61,315 at P 16 (2005). *See also supra* note 139 (listing recent Commission cases approving RMR agreements).

205. Finally, we reject Objecting Parties' contention that ISO-NE may not make a proposal to correct the flaws in the existing capacity market. The provisions pertaining to the existing capacity market are contained in ISO-NE's tariff, and ISO-NE is the entity that is responsible under the NEPOOL Agreement for administering the regional markets. As a result, it is the proper entity to propose remedies to address the identified deficiencies in the current capacity market. In any event, the Settlement Agreement achieved a 78.46 percent favorable vote from the NEPOOL Participants Committee, far above the percentage vote necessary to permit ISO-NE to file market rule changes.[190]

d. Level of Support for the Settlement Agreement

206. Objecting Parties assert that the level of support for the Settlement Agreement is actually less than it first appears, and that the 78.46 percent vote in favor of the agreement in the NEPOOL stakeholder process masks the level of opposition to the agreement. In particular, they note that both Massachusetts and Maine (representing 53.4 percent of NEPOOL's peak demand) oppose the agreement, as do representatives of load from other states (including the Connecticut Attorney General). They also note that the Alternate Resources, End User and Publicly Owned Entity sectors of NEPOOL represented 40.27 percent of the 78.46 percent vote in favor (or more than 50 percent of the total NEPOOL support). According to Objecting Parties, due to flaws in the membership of these sectors, and the disproportionate weight

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[190] *See* NEPOOL Participants Agreement, section 11.

given to the Publicly Owned Entity sector, true customer satisfaction with the settlement is misrepresented.[191]

207. NEPOOL states in reply that Objecting Parties' assertions regarding the opposition of Massachusetts and Maine are factually misleading. In fact, NEPOOL argues, most of the Massachusetts parties either support or did not oppose the Settlement Agreement, including Associated Industries of Massachusetts (representing the largest energy consumers in Massachusetts), transmission-owning utilities National Grid USA and Western Massachusetts Electric Company, and 38 publicly-owned entities. Similarly, Capacity Suppliers note that the Massachusetts Department of Telecommunications and Energy did not file comments in opposition to the settlement, nor did many of the load-serving entities in Massachusetts. NEPOOL notes that two distribution companies in Maine (Central Maine Power and Bangor Hydro Electric Company) did not file any comments in opposition, thus waiving any opposition they may have. NEPOOL notes that no competitive supplier from Massachusetts or Maine has filed comments in opposition. Further, it contends that Objecting Parties' statement that parties representing load from other states also oppose the settlement completely ignores the support of state regulators in Connecticut, New Hampshire, Rhode Island and Vermont, as well as the fact that the Connecticut Office of Consumer Counsel (the statutory representative of retail customers in Connecticut) is a settling party. Last, NEPOOL argues that the voting structure that Objecting Parties now challenge was created at the insistence of the Commission to ensure that individual entities like NSTAR would not have disproportionate voting weight, and that this structure

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[191] *See* Comments in Opposition to Settlement of Objecting Parties at 14-16.

represents a rejection of Objecting Parties' implicit argument that NEPOOL voting should be more reflective of economic interests.[192]

208. CMEEC and MMWEC characterize Objecting Parties' arguments as a collateral attack on the NEPOOL voting process, and argue that it should play no role in the Commission's decision on the Settlement Agreement.[193] If the Commission decides to consider these issues, CMEEC notes that it also shares concerns with regard to the NEPOOL stakeholder process, arguing (in contrast to Objecting Parties) that the process gives too little weight to consumer interests and too much weight to sectors populated by investor-owned companies whose interest is to maximize shareholder returns and not ensure just and reasonable rates.

Commission Conclusion

209. We reject Objecting Parties' attacks on the NEPOOL stakeholder process and the NEPOOL stakeholder vote in favor of the settlement. Objecting Parties' arguments are misplaced. As NEPOOL, CMEEC and MMWEC correctly point out, those stakeholder processes were confirmed in other Commission proceedings, and issues regarding their effectiveness or fairness are outside the scope of this proceeding.

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[192] Reply Comments of NEPOOL at 9, *citing New England Power Pool*, 86 FERC ¶ 61,262 (1999).

[193] MMWEC also states that this stakeholder process was approved by the Commission in *New England Power Pool*, 88 FERC ¶ 61,079 (1999), and reconfirmed when the Commission approved New England's RTO arrangements in *ISO New England, Inc.*, 106 FERC ¶ 61,280 (2004).

The Commission orders:

The proposed Settlement Agreement is hereby accepted, as discussed in the body of this order.

By the Commission. Commissioner Kelly concurring with a separate statement attached.

(SEAL)

Magalie R. Salas,
Secretary.

Appendix A – List of Settling Parties

American National Power, Inc.
Associated Industries of Massachusetts
Boston Generating, LLC
Calpine Eastern Corporation
Calpine Energy Services, L.P.
Cape Wind Associates, LLC
Central Vermont Public Service Corporation
Connecticut Department of Public Utility Control
The Connecticut Light and Power Company
Connecticut Municipal Electric Energy Cooperative
Connecticut Office of Consumer Counsel
Conservation Services Group
Consolidated Edison Energy, Inc.
Dominion Energy Marketing, Inc.
Dominion Nuclear Connecticut, Inc.
Dominion Resources, Inc.
Duke Energy North America, LLC
Energy Management, Inc.
EnerNOC, Inc.
Entergy Nuclear Generation Company
Entergy Nuclear Vermont Yankee, LLC
Exelon Generation Company, LLC
Exelon New England Holdings, LLC
Fitchburg Gas & Electric Light Company
FFL Energy, LLC
Granite Ridge Energy, LLC
HQ Energy Services (U.S.), Inc.
ISO New England, Inc.
Lake Road Generating Company, LP
Long Island Power Authority (LIPA)
MASSPOWER
Milford Power Company, LLC
Mirant Americas Energy Marketing, LP
Mirant Canal, LLC
Mirant Kendall, LLC

Mystic Development, LLC, Mystic I, LLC. and Fore River Development, LLC
National Grid USA (on behalf of itself and its subsidiaries that are intervenors in this proceeding)
NEPOOL Participants Committee
New Hampshire Electric Cooperative, Inc.
New Hampshire Office of Consumer Advocate
New Hampshire Public Utilities Commission
NRG (Devon Power, LLC. Middletown Power LLC, Montville Power LLC, Norwalk Harbor, LLC, and NRG Power Marketing)
Pinpoint Power
Public Service Company of New Hampshire
RI Division of Public Utilities and Carriers
RI Public Utilities Commission
Select Energy
Sempra Trading
TransCanada Power Marketing Limited
The United Illuminating Company
Vermont Department of Public Service
Vermont Public Power Supply Authority
Vermont Public Service Board

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Devon Power LLC Docket Nos. ER03-563-030
ER03-563-055

(Issued June 16, 2006)

KELLY, Commissioner, *concurring*:

Price mitigation in energy markets, coupled with capacity payments that did not recognize transmission limitations that prevent some generation from reaching some areas and lack of adequate transmission investment to address those limitations, ultimately led to increased proliferation of cost-based RMR agreements as generation that should have been permitted to retire had to be kept on for local reliability. The Commission issued orders finding the existing situation unjust and unreasonable and directing ISO-NE to propose a solution. In response, ISO-NF developed the LICAP proposal with its sloping demand curve and other features. The proposal stirred up great controversy and even Congress addressed it in the Energy Policy Act of 2005.

Following the ALJ's issuance of the LICAP initial decision, we granted requests to hold an oral argument on LICAP and on proposed alternatives and ultimately delayed issuance of an Opinion on the initial decision pending the outcome of settlement procedures among the parties.

To my surprise and delight the vast majority of the parties reached a settlement that they believe will meet their broad and varied interests in an acceptable manner. Moreover, my examination of their settlement proposal shows it to be a balanced and reasonable way to address the underlying problems the Commission identified in earlier orders.

For these reasons, I am pleased to be able to vote for this settlement despite the fact that it includes a limited application of the Mobile-Sierra public interest standard. For the reasons I have previously set forth in *Wisconsin Power & Light Co.*, 106 FERC ¶ 61,112 (2004), I do not generally believe that the Commission should depart from its precedent of not approving settlement provisions that preclude the Commission, acting *sua sponte* on behalf of a non-party, or pursuant to a complaint by a non-party, from investigating rates, terms and conditions under the "just and reasonable" standard of section 206 of the Federal Power Act at such times and under such circumstances as the Commission deems appropriate. Therefore, I have generally dissented in part from orders that accept for filing settlements that provide that the "public interest" standard of review will apply to Commission action pursuant to section 206. However, I believe that no such dissent is warranted here due to the settling parties' decision to apply the *Mobile-Sierra* public interest standard in a very constrained and time-limited manner; specifically, applying it only to the stated transition period prices and the annual prices generated each year by the FCM auctions. Customers are protected due to the time-limited nature of this application and the fact that everything else is covered by the just and reasonable standard.

Suedeen G. Kelly

APPENDIX D

UNITED STATES OF AMERICA FEDERAL ENERGY REGULATORY COMMISSION

NOS. 06-1403 *et al.*

MAINE PUBLIC UTILITIES COMMISSION, RICHARD BLUMENTHAL, ATTORNEY GENERAL FOR THE STATE OF CONNECTICUT, AND MARTHA COAKLEY, ATTORNEY GENERAL FOR MASSACHUSETTS,
Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondents.

(August 4, 2008)

KELLY and WELLINGHOFF, Commissioners, *dissenting*:

We dissent from the Commission's decision to seek rehearing of the portion of the decision in *Maine Public Utilities Commission v. FERC*, 520 F.3d 464 (D.C. Cir. 2008) (*Maine PUC*) that concerns the applicability of the *Mobile-Sierra* doctrine to the rights of parties who do not agree to settlement in a Commission adjudication. Rehearing is not appropriate because (1) *Maine PUC* does not conflict with the U.S. Supreme Court decision in *Morgan Stanley Capital Group, Inc. v. Public Utility District No. 1 of Snohomish County*, Nos. 06-1457, *et al.* (U.S. Supreme Court June 26, 2008) (*Morgan Stanley*); (2) The *Maine PUC* court did not misapprehend the law,

and its decision therefore is consistent with *Morgan Stanley*; and (3) *Maine PUC* does not damage the Commission's ability to approve settlements in contested proceedings before the Commission.

I. *Maine PUC* does not conflict with *Morgan Stanley*

Maine PUC does not conflict with *Morgan Stanley* because neither *Morgan Stanley*'s holding nor the reasoning supporting it applies to the type of agreement at issue in *Maine PUC*. Further, there is no basis in law or policy to expand the holding in *Morgan Stanley* to settlement agreements in contested adjudications before the Commission.

A. Neither *Morgan Stanley*'s holding nor the reasoning supporting it applies to the type of agreement at issue in *Maine PUC*

Morgan Stanley holds that whenever the Commission reviews a particular type of contract, the Federal Power Act (FPA) requires it to apply the presumption that the contract meets the "just and reasonable" requirement imposed by the act. This presumption (called the *Mobile-Sierra* presumption) may be overcome only if the Commission concludes "that the contract seriously harms the public interest." Slip op. at 1 (citing *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332 (1956) (*Mobile*); *FPC v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956) (*Sierra*)). The contracts that are accorded this special application of the "just and reasonable" standard are those "freely negotiated, wholesale-energy [sales] contracts" that were given a special role in the FPA. *Id.* at 1, 2.

The Court explained how this type of contract plays a special role in the FPA: The FPA provides that regulated utilities may file rate schedules or "tariffs" with the Commission to provide service to electricity purchasers on the terms and prices set forth in those tariffs. Uti-

lities must notify the Commission 60 days before the changes are to go into effect, and the Commission will approve the changes if the Commission finds them to be just and reasonable, usually through an adjudicatory process. However, the FPA also permits utilities to set rates with sophisticated, commercial electricity purchasers through bilateral contracts. These contracts are negotiated privately, in the marketplace, outside the Commission's auspices, and some are later filed with the Commission.[1] It is these wholesale-energy sales contracts between sophisticated commercial buyers and sellers "'that depart[] from the scheme of purely tariff-based regulation and . . . [can] be used in ratesetting,'" that must be accorded the *Mobile-Sierra* application of the just and reasonable standard. *Id.* at 2 (quoting *Verizon Communications Inc. v. FCC*, 535 U.S. 467, 479 (2002) (*Verizon*)). The FPA allows this type of contract to "unilaterally set rates." *Id. at* 17 n.3.

The Court made clear that the *Mobile-Sierra* presumption must be applied by the Commission *whenever* such a contract is reviewed. The Court specifically rejected the Ninth Circuit's finding to the contrary. *Id.* at 16. The Ninth Circuit had concluded that "so long as the Commission concludes . . . that a contract rate is just and reasonable when initially filed, the rate will be presumed just and reasonable in future proceedings." *Id.* at 16-17. The Supreme Court disagreed and held that the presumption applies *whenever* the Commission reviews it, including in its initial review. ("[O]nly when the mutually agreed-upon contract rate seriously harms the consuming public may the Commission declare it not to be just

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[1] Contracts executed by sellers with Commission-granted market-based-rate authority with non-affiliated buyers are not filed with the Commission.

and reasonable." *Id.* at 16. This "is the 'sole concern' in a contract case." *Id.* at 17 n. 3.) This is different from the Commission's previous understanding of the law, which it believed required the Commission initially to review a contract under the "ordinary" just and reasonable standard, *i.e.*, without a *Mobile-Sierra* presumption. *Id.* at 15.

Throughout its opinion, the Court reiterates that its holding is based on the important role the FPA has given to these types of contracts: The FPA "permits rates to be set by [a wholesale-energy sales] contract and not just by tariff." *Id.* at 22. These are "contracts that the FPA [has] embraced as an alternative to 'purely tariff-based regulation,'" *Id.* at 19 (quoting *Verizon*, 535 U. S. at 479); "utilities may set rates with individual electric purchasers through bilateral contracts." *Id.* at 2. The FPA "'departed from the scheme of purely tariff-based regulation and acknowledged that contracts between commercial buyers and sellers could be used in ratesetting.'" *Id.* (quoting *Verizon*, 535 U.S. at 479).

The *Morgan Stanley* Court further explained that its holding here, like that in *Sierra*, 350 U.S. 348, is "grounded in the commonsense notion that 'in wholesale markets, the party charging the rate and the party charged [are] often sophisticated businesses enjoying presumptively equal bargaining power, who could be expected to negotiate a 'just and reasonable' rate as between the two of them.'" *Id.* at 17 (quoting *Verizon*, 535 U.S. at 479). Building on that "commonsense notion", the Court expressed concern that "enabling sophisticated parties who weathered market turmoil by entering long-term contracts to renounce those contracts once the storm has passed . . . would reduce the incentive to conclude such contracts in the future." *Id.* at 18. The Court found that this premise and concerns about buyer's or seller's remorse support a requirement that the Commission must

apply a presumption of justness and reasonableness whenever it is called upon to approve such a bilateral contract. The Court also stated that, should such a contract rate later be challenged by a party to it, the contract can only be abrogated in a case of "'unequivocal public necessity'" or "'extraordinary circumstances'". *Id.* at 22 (citations omitted).

The agreement at issue in *Maine PUC* is not at all like the contract before the Court in *Morgan Stanley*. To the contrary, it differs in every fundamental respect from a privately negotiated, voluntary contract for wholesale energy that unilaterally sets a rate between two sophisticated, commercial entities seeking to sell and buy electricity between them and that may be filed, fully and finally drafted and signed, with the Commission. The agreement at issue in *Maine PUC* is a contested settlement agreement addressing a utility's voluminous, complex proposal to revise its tariff substantially to enable it to establish and operate a locational installed electricity capacity market for the general public. While a voluntary, bilateral, buy-sell contract for wholesale-energy is essentially a private contract that is negotiated in the marketplace, outside the ambit of the regulator, the agreement at issue in *Maine PUC* emanated from a highly contested adjudicatory proceeding before the Commission and involves a broad, public matter. Further, the agreement is not between two sophisticated actors playing on a level field. No "commonsense notion" would hold that the 115 parties to the adjudication of this matter enjoy presumptively equal bargaining power. It follows that the agreement at issue has no special status under the FPA. It is not an alternative to the Commission's tariff-based regulation of a regional transmission operator; it is an example of the Commission's tariff-based regulatory process, which, as the *Morgan Stanley* Court

explained, is governed by the "ordinary" just and reasonable standard.

The holding of *Morgan Stanley* and the reasoning that supports it does not apply to the agreement at issue in *Maine PUC*.

B. There is no basis in law or policy to expand the holding in *Morgan Stanley* to apply to settlement agreements in contested adjudications before the Commission.

Unlike the type of contracts at issue in *Morgan Stanley*, the agreement at issue in *Maine PUC* is not of a type of agreement that can or should enjoy a statutory presumption that it is just and reasonable, either upon initial review by the Commission or in any subsequent challenge.[2]

The Court in *Morgan Stanley* explained that its holding is a special "*application* of the just-and-reasonable standard to contract rates . . . ([which application can be] referr[ed] to . . . as the "public interest standard.") *Id.* at 6. (citation omitted). As explained above, the Court found the legality of this special application of the just and reasonable standard lies in the special rate-setting role that the FPA gives to freely negotiated, bilateral, wholesale-energy sales contracts.

The FPA gives no role, let alone a special one, to settlement agreements reached by parties to contested

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[2] Although there is no legal basis for providing this type of agreement with a statutory presumption that affects the Commission's authority and responsibility under the just and reasonable standard, there is nothing in law or policy that prevents the parties to the agreement from binding themselves, pursuant to private contract law, to challenges of the agreement based only on a showing of "unequivocal public necessity". In effect, there is no legal prohibition on the parties' compromising their individual rights to the "ordinary" just and reasonable review pursuant to FPA sections 205 or 206, 16 U.S.C. § 824d, 824e (2006).

adjudications before the Commission. Thus, there is no basis in law to expand the holding in *Morgan Stanley* to permit the Commission to apply a special version of the just and reasonable standard of the FPA (e.g., a *Mobile-Sierra* "public interest" standard) to an initial or subsequent review of a settlement agreement from a contested adjudication.

There is also no good policy reason to justify allowing the Commission to hold a settlement agreement to any standard other than the "ordinary" just and reasonable standard. Indeed, such a holding would result in imbuing private parties with regulatory authority heretofore reserved to the Commission; would cause untold uncertainty in future adjudications before the Commission; would be unduly discriminatory to applicants for tariff changes who do not obtain settlement agreements; and would result in a regulatory morass of utility tariff provisions with differing status.

1. *Imbuing private parties with regulatory authority heretofore reserved to the Commission*

Currently, when a utility applies for a tariff change under section 205 of the FPA, the Commission reviews the application, through an administrative adjudication to determine whether it is just and reasonable. If, during the course of the adjudication, one or more other parties enter into a settlement agreement, and the holding of *Morgan Stanley* is extended to this type of "contract," then the settlement agreement must be presumed by the Commission to be just and reasonable. Moreover, the presumption could only be overcome if the Commission were to conclude that the settlement agreement seriously harmed the public interest. This would result in significant decision-making authority being transferred from the Commission to the utility and other private parties entering into the settlement agreement. Such transfer of decision-making authority to private parties is justified

when the agreement being reviewed is a voluntary, bilateral, wholesale-energy sales agreement, which is a private contract that affects no one except the contracting parties. However, this is unjustifiable in situations such as that at issue in *Maine PUC*, where the agreement establishes a locational installed electricity capacity market, essentially a public enterprise.

Further, if the Commission or any non-party to the settlement agreement becomes concerned about changed circumstances, and the *Morgan Stanley* holding has been extended to this type of "contract," the Commission would be unable to require a tariff change to reflect those circumstances absent a finding of "unequivocal public necessity" or "extraordinary circumstances." While this higher standard may be justified where sophisticated, private contracting parties are concerned, it imposes too high a standard in all other circumstances. The *Morgan Stanley* Court carefully described and proscribed the arena in which *Mobile-Sierra* should apply to the Commission's statutory just and reasonable review. That arena should not be expanded.

2. *Causing uncertainty in future adjudications before the Commission*

Were the *Morgan Stanley* holding to be extended to the agreement at issue in *Maine PUC*, it would cause great uncertainty in future adjudications before the Commission. The agreement in *Maine PUC* is a settlement of an adjudication that 107 of the 115 parties to the proceeding signed. If the *Mobile-Sierra* standard is applied to this settlement, what does it mean for future settlements? Would it apply to any settlement arrived at by the utility with any of the intervening parties? What if the utility achieved the agreement of one party out of 115? How about 50 parties out of 115? How about two parties out of seven? What if the two settling parties were affiliates of the utility? Would a percentage, rather

than numerical, requirement for *Mobile-Sierra* status be acceptable? How about a requirement that 90 percent of the parties have to sign the agreement to get *Mobile-Sierra* "protection"? If 90 percent is the requirement, then can the individual members of an organization intervene in their individual capacities in order to reach the 90 percent number? The gaming scenarios this could spawn are countless. The uncertainty would be boundless.

3. *Undue discrimination concerns*

Under current law, when a utility applies under section 205 of the FPA for a tariff change, the Commission reviews the filing through an administrative adjudication to determine whether it is just and reasonable. If the *Morgan Stanley* holding is extended to provide for a "public interest" standard of review of any settlement agreement in an adjudicated proceeding, this presents undue discrimination concerns. For example, what if no party intervenes in the proceeding? In such a case, the utility is "prevented" from getting a settlement agreement and, presumably, its requested tariff change is evaluated under the "ordinary" just and reasonable standard. Isn't it unduly discriminatory to hold a utility that has received no opposition to its proposal to a higher burden than a utility whose proposal was opposed but who resolved the opposition through a settlement agreement? If it is undue discrimination to do so, then should the utility that had no intervenor be presumed, in the absence of any objection, to have a settlement agreement? If so, then when does a utility's proposal ever receive the scrutiny of the "ordinary" just and reasonable standard that Congress contemplated? If not, then will the utility manufacture specious opposition solely to secure a settlement agreement?

4. *Resulting regulatory morass of utility tariff provisions with differing status*

Many adjudicatory proceedings before the Commission, like the one giving rise to *Maine PUC*, concern utility proposals under section 205 of the FPA to amend their tariffs. If this court were to permit settlement agreements in these cases to carry with them just and reasonable presumptions that can only be overcome if the Commission concludes that a provision in the agreement seriously harms the public interest, this will lead to a regulatory morass in future proceedings insofar as changes to tariff provisions are involved.

Currently, if the Commission or any person other than the utility with the tariff provision wishes to change a tariff provision, it must prove that the provision at issue is unjust, unreasonable, unduly discriminatory or preferential. 16 U.S.C. § 824e(a) (2006). If tariff provisions that have been established through settlement agreements have a special status different from the status of tariff provisions that have not been so established, any process undertaken to reform these tariff provisions will be an exercise in combing through haystacks to determine which of the tariff provisions get special treatment and which do not. And that will be only the beginning of the exercise.

In an actual proceeding to reform tariff provisions, those enjoying special status will only be able to be changed in a case of "unequivocal public necessity" or "extraordinary circumstances," slip op. at 22 (citations omitted), while the others could be changed if they are merely "unjust" or "unreasonable." Multiple tariff provisions frequently coalesce to establish a policy or program—for example, a locational installed capacity market. If, after several years of experience with the market's operation, a case were to arise to consider reform, it may be that some of the tariff provisions at issue will

have special status and others will not. In that case, the reality is that the higher standard will rule the case and no change will be made unless it is in the "unequivocal public necessity." It seems particularly unwise in times of electricity industry and market evolution to make it *more difficult* to make changes to accommodate changing market circumstances.

II. The *Maine PUC* court did not misapprehend the law, and, therefore, its decision is consistent with *Morgan Stanley*

The majority believes that the *Maine PUC* court misapprehended the law. We disagree. *Maine PUC* is consistent with *Morgan Stanley*.

The *Maine PUC* court was faced with a contested settlement agreement concerning a regional transmission operator's request to the Commission to revise its tariff to allow it to establish a locational installed electricity capacity market. As the court noted, the Commission had "approved the settlement agreement, finding that 'as a package, it presents a just and reasonable outcome for this proceeding consistent with the public interest.'" *Maine PUC*, 520 F.3d at 469 (citation omitted). The provisions of the settlement agreement were then incorporated into the regional transmission operator's tariff. Several of the non-settling parties to the adjudication appealed various provisions of the settlement agreement, including one that provided that the Commission was required to apply "the 'public interest' standard, rather than the 'just and reasonable' standard" to "all future challenges to the transition payments and final auction prices 'whether the change is proposed by a Settling Party, a non-Settling Party, or the FERC acting *sua sponte*.'" *Id.* at 476. The non-settling parties argued that this provision "will deprive them of their statutory right to challenge rates under the 'just and reasonable' standard." *Id.* at 477. The court agreed.

The *Maine PUC* court's reasoning is remarkably consistent with the later-issued opinion in *Morgan Stanley*. The court began by explaining that the special treatment provided for under the *Mobile-Sierra* doctrine is reserved to "'freely negotiated private contracts that set firm rates or establish a specific methodology for setting the rates for service.'" *Id.* at 477 (quoting *Atl. City Elec. Co. v. FERC*, 295 F.3d 1, 14 (2002) (*Atl. City*)). Such contracts can only be modified by the Commission "if required by the public interest." *Id.* Compare this with the *Morgan Stanley* holding, as delivered in its first two sentences:

> Under the *Mobile-Sierra* doctrine, the [Commission] must presume that the rate set out in a freely negotiated wholesale-energy [sales] contract meets the 'just and reasonable' requirement imposed by law. The presumption may be overcome only if FERC concludes that the contract seriously harms the public interest. Slip op. at 1.

The *Maine PUC* court continued that the "purpose of the *Mobile-Sierra* doctrine is 'to preserve the benefits of the parties' bargain as reflected in the contract, assuming that there was no reason to question what transpired at the contract formation stage.'" *Maine PUC*, 520 F.3d at 477 (quoting *Atl.City*, 295 F.3d at 14). Compare this with the *Morgan Stanley* Court's explanation that "the principal regulatory responsibility is not to relieve a contracting party of an unreasonable rate", but rather that "FERC has ample authority to set aside a contract where there is unfair dealing at the contract formation stage." Slip op. at 6, 19.

The *Maine PUC* court explained that the *Mobile-Sierra* doctrine "applies a more deferential standard of review to preserve the terms of the bargain as between the contracting parties," and the *Mobile-Sierra* protection afforded such contracts "departs from the usual 'just

and reasonable' standard and makes it harder" for a party to the contract subsequently to "successfully challenge the rate in cases of changed circumstances." *Maine PUC*, 520 F.3d at 478. Compare this with the *Morgan Stanley* Court's explanation that

> the term 'public interest standard' refers to the differing *application* of the just-and-reasonable standard to contract rates. (It would be less confusing to adopt the Solicitor General's terminology, referring to the two differing applications of the just-and-reasonable standard as the "ordinary" "just and reasonable standard" and the "public interest standard.") Slip op. at 6 (citation omitted).

Thus, the *Maine PUC* interpretation of the *Mobile-Sierra* doctrine is completely consistent with *Morgan Stanley*.

The *Maine PUC* court, faced with a contested settlement agreement concerning tariff provisions proposed to establish a locational electricity capacity market, rather than a voluntarily negotiated, bilateral wholesale-energy sales agreement between two sophisticated commercial parties, went on to make the unsurprising finding that the "contract" before it was not of the type that qualifies for the special treatment afforded by *Mobile-Sierra*:

> This case is clearly outside the scope of the *Mobile-Sierra* doctrine. As we explained, *Mobile-Sierra* is invoked when "one party to a rate contract on file with FERC attempts to effect a unilateral rate change by asking FERC to relieve its obligations under a contract whose terms are no longer favorable to that party." *Maine PUC*, 520 F.3d at 477-78 (quoting *Maine PUC*, 454 F.3d 278, 284 (2006)).

This holding is entirely consistent with the holding in *Morgan Stanley*, which, as explained above, limits the special *Mobile-Sierra* type contract review treatment to voluntarily and privately negotiated, bilateral wholesale-energy buy/sell agreements between sophisticated parties that unilaterally set a rate between them alone.

III. *Maine PUC* does not damage the Commission's ability to approve settlements of contested proceedings before the Commission

By holding that the contested settlement in *Maine PUC* is outside the scope of the *Mobile-Sierra* doctrine, the court essentially preserves Congressional intent as set out in section 205 of the FPA, to require the Commission to apply the "ordinary" just and reasonable standard when considering any settlement in a contested adjudication of a proposed tariff revision. This holding is consistent with the Commission's long-standing practice. However, if the court were to grant rehearing of *Maine PUC* and extend *Morgan Stanley* beyond the type of bilateral contracts discussed above, then the Commission would need to change this practice and apply a presumption of justness and reasonableness to such settlement agreements.

The *Maine PUC* holding also preserves Congress' decision, as set out in section 206 of the FPA, to allow utility tariff provisions, whether arrived at through settlement agreements or not, to be challenged in the event of future changed circumstances by complainants or the Commission acting *sua sponte* under the "ordinary" just and reasonable standard.

We believe the *Maine PUC* holding is not only the correct legal outcome, but also the best policy outcome. The majority disagrees. It believes that unless the law allows parties to a contested settlement who have agreed among themselves to compromise their FPA section 206

rights[3] to impose this compromise on non-settling parties, as well as on the Commission acting *sua sponte*, the Commission's ability to approve settlements in the future will be "seriously damaged". The majority also expresses concern that this will "undermine" the Commission's ability to provide "a degree of future rate certainty." We do not share those concerns.

Starting with the second concern, we believe that the just and reasonable standard is rigorous, in and of itself, and not easily satisfied by challengers. In order to change a utility tariff provision that has been approved by the Commission under the just and reasonable standard, a challenger or the Commission acting *sua sponte* must prove that circumstances have changed so dramatically that the tariff provision has become unjust and unreasonable. This does not happen often.

Second, the fact that parties to a contested adjudication before the Commission have the legal right to compromise their FPA section 205 and 206 rights to limit their own future challenges to the tariff provisions gives them substantial control over the future certainty of the provisions. The greater number of parties to an adjudication who can be brought to the negotiation table to compromise their statutory challenge rights, the smaller the universe of persons who can mount a challenge under the "ordinary" just and reasonable standard. Further, this provides an incentive to negotiate a broad settlement—an incentive that is not provided if any settling party could bind all non-settling parties. The broader the settlement, the more likely it is to be just and reasonable to all involved and in the broader public interest.

Finally, when parties to a settlement agreement choose to limit their challenge rights, it has an impact on

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[3] In the case of the utility, it would be its FPA section 205 right.

the Commission as a decision-maker, providing potent evidence that they so strongly believe this is the best course for them that they are willing to sign away valuable rights. Such evidence matters as the Commission engages in its statutorily required deliberation whether the tariff is just and reasonable.

Regarding the majority's concern that the inability of settling parties to bind non-settling parties and the Commission acting *sua sponte* to a standard higher than the "ordinary" just and reasonable standard will somehow damage the Commission's ability to approve settlements, we simply fail to see why that would occur. What will otherwise settling parties do upon being apprised that they cannot legally bind non-settling parties to their agreement? It seems that they will do one of two things. To the extent they highly value almost-absolute-future-certainty, and to the extent they believe that having the non-settling parties compromise their FPA section 206 rights is necessary to achieve that high degree of certainty, they will compromise other aspects of the settlement to get non-settling parties to agree to it. To the extent they do not value absolute certainty more highly than other aspects of the settlement, they will not compromise the other aspects of the settlement. It does not seem at all likely, however, that this issue will result in no settlement at all. The objective is maximum certainty, and failing to reach a settlement provides none.

For these reasons, as well as for the policy reasons we discussed above, we do not believe that *Maine PUC* damages the ability of the Commission to approve settlements. In fact, we believe its holding will provide more, not fewer, incentives for parties to a contested adjudication to settle the issues among themselves.

For all of the reasons we have enumerated above, we respectfully dissent.

Suedeen G. Kelly	Jon Wellinghoff
Commissioner	Commissioner

APPENDIX E

IN THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 06-1403

FERC-ER03-563-060

Consolidated with 06-1427, 07-1193

MAINE PUBLIC UTILITIES COMMISSION,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent.

CONNECTICUT DEPARTMENT OF PUBLIC UTILITY CONTROL, *et al.*,
Intervenors.

SEPTEMBER TERM 2008

FILED ON: OCTOBER 6, 2008

BEFORE: Rogers and Garland, Circuit Judges, and Silberman, Senior Circuit Judge

ORDER

Upon consideration of the petition of intervenors Entergy Nuclear Generation Co., *et al.*, for panel rehearing filed on August 11, 2008, it is

ORDERED that the petition be denied.

Per Curiam

FOR THE COURT:
Mark J. Langer, Clerk

BY: /s/
Michael C. McGrail
Deputy Clerk

APPENDIX F

IN THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 06-1403

FERC-ER03-563-060

Consolidated with 06-1427, 07-1193

MAINE PUBLIC UTILITIES COMMISSION,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent.

CONNECTICUT DEPARTMENT OF PUBLIC UTILITY CONTROL, *et al.*,
Intervenors.

SEPTEMBER TERM 2008

FILED ON: OCTOBER 6, 2008

BEFORE: Rogers and Garland, Circuit Judges, and Silberman, Senior Circuit Judge

ORDER

Upon consideration respondent's petition for panel rehearing filed on August 8, 2008, it is

ORDERED that the petition be denied.

Per Curiam

FOR THE COURT:
Mark J. Langer, Clerk

BY: /s/
Michael C. McGrail
Deputy Clerk

APPENDIX G

IN THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 06-1403

FERC-ER03-563-060

Consolidated with 06-1427, 07-1193

MAINE PUBLIC UTILITIES COMMISSION,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent.

CONNECTICUT DEPARTMENT OF PUBLIC UTILITY CONTROL, *et al.*,
Intervenors.

SEPTEMBER TERM 2008

FILED ON: OCTOBER 6, 2008

BEFORE: Sentelle, Chief Judge, and Ginsburg,* Henderson,* Randolph, Rogers, Tatel, Garland, Brown, Griffith, and Kavanaugh, Circuit Judges, and Silberman, Senior Circuit Judge

ORDER

Upon consideration of the petition of intervenors Entergy Nuclear Generation Co., et al., for rehearing en banc, the response thereto, and the absence of a request by any member of the court for a vote, it is

ORDERED that the petition be denied.

Per Curiam

FOR THE COURT:
Mark J. Langer, Clerk

BY: /s/
Michael C. McGrail
Deputy Clerk

* Circuit Judges Ginsburg and Henderson did not participate in this matter.

APPENDIX H

IN THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 06-1[illegible]3

FERC-ER03-563-060

Consolidated with 06-1427, 07-1193

MAINE PUBLIC UTILITIES COMMISSION,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent.

CONNECTICUT DEPARTMENT OF PUBLIC UTILITY CONTROL, *et al.*,
Intervenors.

SEPTEMBER TERM 2008

FILED ON: OCTOBER 6, 2008

BEFORE: Sentelle, Chief Judge, and Ginsburg,* Henderson,* Randolph, Rogers, Tatel, Garland, Brown, Griffith, and Kavanaugh, Circuit Judges, and Silberman, Senior Circuit Judge

ORDER

Upon consideration of respondent's petition for rehearing en banc, the response thereto, and the absence of a request by any member of the court for a vote, it is

ORDERED that the petition be denied.

Per Curiam

FOR THE COURT:
Mark J. Langer, Clerk

BY: /s/
Michael C. McGrail
Deputy Clerk

* Circuit Judges Ginsburg and Henderson did not participate in this matter.

APPENDIX I

IN THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 06-1403
FERC-ER06-1465-001
FERC-ER03-563-060
Consolidated with 06-1427, 07-1193

MAINE PUBLIC UTILITIES COMMISSION,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent.

CONNECTICUT DEPARTMENT OF PUBLIC UTILITY CONTROL, *et al.*,
Intervenors.

SEPTEMBER TERM 2007
FILED ON: AUGUST 22, 2008

ORDER

Upon consideration of the petitions of respondent and intervenors for respondent for rehearing and rehearing en banc, it is

ORDERED, on the court's own motion, that, within 15 days of the date of this order, petitioners and intervenors for petitioners file a joint response, not to exceed 15

pages. Absent further order of the court, the court will not accept a reply to the response.

FOR THE COURT:
Mark J. Langer, Clerk

BY: /s/
Nancy G. Dunn
Deputy Clerk

APPENDIX J

RELEVANT STATUTORY PROVISIONS

The Federal Power Act ("FPA"), Public Utility Act of 1935, tit. II, ch. 687, 49 Stat. 803, 838-63 codified as amended at 16 U.S.C. §§ 791a-825r, provides, in relevant part:

§ 824d. Rates and charges; schedules; suspension of new rates; automatic adjustment clauses

(a) Just and reasonable rates

All rates and charges made, demanded, or received by any public utility for or in connection with the transmission or sale of electric energy subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) Preference or advantage unlawful

No public utility shall, with respect to any transmission or sale subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Schedules

Under such rules and regulations as the Commission may prescribe, every public utility shall file with the Commission, within such time and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection schedules showing all rates and charges for any transmission or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which

in any manner affect or relate to such rates, charges, classifications, and services.

(d) Notice required for rate changes

Unless the Commission otherwise orders, no change shall be made by any public utility in any such rate, charge, classification, or service, or in any rule, regulation, or contract relating thereto, except after sixty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the sixty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Suspension of new rates; hearings; five-month period

Whenever any such new schedule is filed the Commission shall have authority, either upon complaint or upon its own initiative without complaint, at once, and, if it so orders, without answer or formal pleading by the public utility, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the public utility affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect; and after full hearings, either completed before or after

the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of such five months, the proposed change of rate, charge, classification, or service shall go into effect at the end of such period, but in case of a proposed increased rate or charge, the Commission may by order require the interested public utility or public utilities to keep accurate account in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts are paid, and upon completion of the hearing and decision may by further order require such public utility or public utilities to refund, with interest, to the persons in whose behalf such amounts were paid, such portion of such increased rates or charges as by its decision shall be found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the public utility, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible.

(f) Review of automatic adjustment clauses and public utility practices; action by Commission; "automatic adjustment clause" defined

(1) Not later than 2 years after November 9, 1978, and not less often than every 4 years thereafter, the Commission shall make a thorough review of automatic adjustment clauses in public utility rate schedules to examine—

(A) whether or not each such clause effectively provides incentives for efficient use of resources (including economical purchase and use of fuel and electric energy), and

(B) whether any such clause reflects any costs other than costs which are--

(i) subject to periodic fluctuations and

(ii) not susceptible to precise determinations in rate cases prior to the time such costs are incurred.

Such review may take place in individual rate proceedings or in generic or other separate proceedings applicable to one or more utilities.

(2) Not less frequently than every 2 years, in rate proceedings or in generic or other separate proceedings, the Commission shall review, with respect to each public utility, practices under any automatic adjustment clauses of such utility to insure efficient use of resources (including economical purchase and use of fuel and electric energy) under such clauses.

(3) The Commission may, on its own motion or upon complaint, after an opportunity for an evidentiary hearing, order a public utility to—

(A) modify the terms and provisions of any automatic adjustment clause, or

(B) cease any practice in connection with the clause,

if such clause or practice does not result in the economical purchase and use of fuel, electric energy, or other items, the cost of which is included in any rate schedule under an automatic adjustment clause.

(4) As used in this subsection, the term "automatic adjustment clause" means a provision of a rate schedule which provides for increases or decreases (or both), without prior hearing, in rates reflecting increases or decreases (or both) in costs incurred by an electric utility. Such term does not include any rate which takes effect subject to refund and subject to a later determination of the appropriate amount of such rate.

§ 824e. Power of Commission to fix rates and charges; determination of cost of production or transmission

(a) Unjust or preferential rates, etc.; statement of reasons for changes; hearing; specification of issues

Whenever the Commission, after a hearing held upon its own motion or upon complaint, shall find that any rate, charge, or classification, demanded, observed, charged, or collected by any public utility for any transmission or sale subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order. Any complaint or motion of the Commission to initiate a proceeding under this section shall state the change or changes to be made in the rate, charge, classification, rule, regulation, practice, or contract then in force, and the reasons for any proposed change or changes therein. If, after review of any motion or complaint and answer, the Commission shall decide to hold a hearing, it shall fix by order the time and place of such hearing and shall specify the issues to be adjudicated.

(b) Refund effective date; preferential proceedings; statement of reasons for delay; burden of proof; scope of refund order; refund orders in cases of dilatory behavior; interest

Whenever the Commission institutes a proceeding under this section, the Commission shall establish a refund effective date. In the case of a proceeding instituted on complaint, the refund effective date shall not be earlier than the date of the filing of such complaint nor later

than 5 months after the filing of such complaint. In the case of a proceeding instituted by the Commission on its own motion, the refund effective date shall not be earlier than the date of the publication by the Commission of notice of its intention to initiate such proceeding nor later than 5 months after the publication date. Upon institution of a proceeding under this section, the Commission shall give to the decision of such proceeding the same preference as provided under section 824d of this title and otherwise act as speedily as possible. If no final decision is rendered by the conclusion of the 180-day period commencing upon initiation of a proceeding pursuant to this section, the Commission shall state the reasons why it has failed to do so and shall state its best estimate as to when it reasonably expects to make such decision. In any proceeding under this section, the burden of proof to show that any rate, charge, classification, rule, regulation, practice, or contract is unjust, unreasonable, unduly discriminatory, or preferential shall be upon the Commission or the complainant. At the conclusion of any proceeding under this section, the Commission may order refunds of any amounts paid, for the period subsequent to the refund effective date through a date fifteen months after such refund effective date, in excess of those which would have been paid under the just and reasonable rate, charge, classification, rule, regulation, practice, or contract which the Commission orders to be thereafter observed and in force: *Provided*, That if the proceeding is not concluded within fifteen months after the refund effective date and if the Commission determines at the conclusion of the proceeding that the proceeding was not resolved within the fifteen-month period primarily because of dilatory behavior by the public utility, the Commission may order refunds of any or all amounts paid for the period subsequent to the refund effective date and prior to the conclusion of the pro-

ceeding. The refunds shall be made, with interest, to those persons who have paid those rates or charges which are the subject of the proceeding.

(c) Refund considerations; shifting costs; reduction in revenues; "electric utility companies" and "registered holding company" defined

Notwithstanding subsection (b) of this section, in a proceeding commenced under this section involving two or more electric utility companies of a registered holding company, refunds which might otherwise be payable under subsection (b) of this section shall not be ordered to the extent that such refunds would result from any portion of a Commission order that (1) requires a decrease in system production or transmission costs to be paid by one or more of such electric companies; and (2) is based upon a determination that the amount of such decrease should be paid through an increase in the costs to be paid by other electric utility companies of such registered holding company: *Provided*, That refunds, in whole or in part, may be ordered by the Commission if it determines that the registered holding company would not experience any reduction in revenues which results from an inability of an electric utility company of the holding company to recover such increase in costs for the period between the refund effective date and the effective date of the Commission's order. For purposes of this subsection, the terms "electric utility companies" and "registered holding company" shall have the same meanings as provided in the Public Utility Holding Company Act of 1935, as amended [15 U.S.C.A. § 79 et seq.].

(d) Investigation of costs

The Commission upon its own motion, or upon the request of any State commission whenever it can do so without prejudice to the efficient and proper conduct of its affairs, may investigate and determine the cost of the

production or transmission of electric energy by means of facilities under the jurisdiction of the Commission in cases where the Commission has no authority to establish a rate governing the sale of such energy.

(e)(1) In this subsection:

(A) The term "short-term sale" means an agreement for the sale of electric energy at wholesale in interstate commerce that is for a period of 31 days or less (excluding monthly contracts subject to automatic renewal).

(B) The term "applicable Commission rule" means a Commission rule applicable to sales at wholesale by public utilities that the Commission determines after notice and comment should also be applicable to entities subject to this subsection.

(2) If an entity described in section 824(f) of this title voluntarily makes a short-term sale of electric energy through an organized market in which the rates for the sale are established by Commission-approved tariff (rather than by contract) and the sale violates the terms of the tariff or applicable Commission rules in effect at the time of the sale, the entity shall be subject to the refund authority of the Commission under this section with respect to the violation.

(3) This section shall not apply to—

(A) any entity that sells in total (including affiliates of the entity) less than 8,000,000 megawatt hours of electricity per year; or

(B) an electric cooperative.

(4)(A) The Commission shall have refund authority under paragraph (2) with respect to a voluntary short term sale of electric energy by the Bonneville Power Administration only if the sale is at an unjust and unreasonable rate.

(B) The Commission may order a refund under subparagraph (A) only for short-term sales made by the Bonneville Power Administration at rates that are higher than the highest just and reasonable rate charged by any other entity for a short-term sale of electric energy in the same geographic market for the same, or most nearly comparable, period as the sale by the Bonneville Power Administration.

(C) In the case of any Federal power marketing agency or the Tennessee Valley Authority, the Commission shall not assert or exercise any regulatory authority or power under paragraph (2) other than the ordering of refunds to achieve a just and reasonable rate.

* * *

§ 825*l*. Review of orders

(a) Application for rehearing; time periods; modification of order

Any person, electric utility, State, municipality, or State commission aggrieved by an order issued by the Commission in a proceeding under this chapter to which such person, electric utility, State, municipality, or State commission is a party may apply for a rehearing within thirty days after the issuance of such order. The application for rehearing shall set forth specifically the ground or grounds upon which such application is based. Upon such application the Commission shall have power to grant or deny rehearing or to abrogate or modify its order without further hearing. Unless the Commission acts upon the application for rehearing within thirty days after it is filed, such application may be deemed to have been denied. No proceeding to review any order of the Commission shall be brought by any entity unless such entity shall have made application to the Commission for a rehearing thereon. Until the record in a proceeding shall have been filed in a court of appeals, as provided in

subsection (b) of this section, the Commission may at any time, upon reasonable notice and in such manner as it shall deem proper, modify or set aside, in whole or in part, any finding or order made or issued by it under the provisions of this chapter.

(b) Judicial review

Any party to a proceeding under this chapter aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the United States Court of Appeals for any circuit wherein the licensee or public utility to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall forthwith be transmitted by the clerk of the court to any member of the Commission and thereupon the Commission shall file with the court the record upon which the order complained of was entered, as provided in section 2112 of Title 28. Upon the filing of such petition such court shall have jurisdiction, which upon the filing of the record with it shall be exclusive, to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceedings before

the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings which, if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the Commission, shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in section 1254 of Title 28.

(c) Stay of Commission's order

The filing of an application for rehearing under subsection (a) of this section shall not, unless specifically ordered by the Commission, operate as a stay of the Commission's order. The commencement of proceedings under subsection (b) of this section shall not, unless specifically ordered by the court, operate as a stay of the Commission's order.

OPPOSITION BRIEF

23

(3)

No. 08-674

FILED

MAR 18 2009

OFFICE OF THE CLERK
SUPREME COURT, U.S.

In The

Supreme Court of the United States

NRG POWER MARKETING, LLC, ET AL.,

Petitioners,

v.

MAINE PUBLIC UTILITIES COMMISSION, ET AL.,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The District Of Columbia Circuit

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QUESTION PRESENTED

Section 206 of the Federal Power Act ("FPA"), 16 U.S.C. § 824e(a), requires that all rates for the transmission and sale of electricity in interstate commerce must be "just and reasonable." Under the *Mobile-Sierra* doctrine, when sellers and purchasers enter into freely negotiated wholesale energy contracts, the Federal Energy Regulatory Commission ("FERC" or "Commission") must presume that the negotiated rate is just and reasonable, and parties to the contract may overcome that presumption only by showing that the contract seriously harms the "public interest." In this case, some but not all parties to a contested FERC proceeding had entered into a settlement agreement in a contested proceeding. The contested settlement purported to apply the restrictive *Mobile-Sierra* presumption to challenges by non-settling parties to rates that will be determined in the future.

The question presented is:

Whether the Commission may deprive non-settling parties of their statutory right under the FPA to challenge rates upon a showing that the rates are not "just and reasonable," by approving a settlement agreement that would require rate challenges brought by non-settling third parties to be evaluated under the much more stringent "public interest" mode of review.

CORPORATE DISCLOSURE STATEMENT

Richard Blumenthal, Attorney General for the State of Connecticut ("CTAG") hereby submits that the Office of the Attorney General is a governmental party exempt from any reporting requirement under Rule 29.6. The CTAG is the chief civil legal officer of the State of Connecticut and has no parent corporation or publicly held stock.

The Maine Public Utilities Commission ("MPUC") hereby submits that it is a governmental party exempt from any reporting requirement under Rule 29.6. MPUC has no parent corporation or publicly held stock.

Martha Coakley, Attorney General for the Commonwealth of Massachusetts ("MassAG"), hereby submits that the Office of the Attorney General is a governmental party exempt from any reporting requirement under Rule 29.6. The MassAG is the chief civil legal officer of the Commonwealth of Massachusetts and has no parent corporation or publicly held stock.

The Industrial Energy Consumer Group ("IECG") is a non-profit trade association incorporated under the laws of the State of Maine. The IECG has no parent company or affiliated companies. The IECG was created and exists to advance the interests of industrial users of electricity in Maine and other interested persons. There are no ownership interests associated with the IECG.

CORPORATE DISCLOSURE STATEMENT – Continued

NEPOOL Industrial Customer Coalition ("NICC") is a continuing ad hoc association of large industrial and commercial end-users of electricity in New England operated for the purposes of representing the interests of industrial energy consumers before regulatory and legislative bodies. NICC does not issue securities to the public and is not owned by any publicly held company.

NSTAR Electric & Gas Corporation is a wholly-owned subsidiary of NSTAR, a public utility holding company which has issued securities to the public. In addition, NSTAR Electric & Gas Corporation's affiliate, NSTAR Electric Company, has issued preferred stock and debt securities to the public. No other affiliates of NSTAR Electric & Gas Corporation have outstanding securities to the public.

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STATEMENT OF THE CASE

This case involves "a comprehensive settlement that redesigned New England's capacity market" for electricity. Pet. App. 1a. A unanimous panel of the D.C. Circuit concluded that eight parties that opposed the agreement are not bound by a provision which purported to impose a stringent public-interest showing on future challenges to future prices for electric generation capacity. The court correctly found that the settlement's opponents did not waive or otherwise lose their rights to challenge the future prices under the ordinary application of the just-and-reasonable standard. That commonsense holding does not conflict with the holding of any other court.

Petitioners' effort to cast this case as a logical follow-up to *Morgan Stanley Capital Group Inc. v. Public Utility District No. 1*, 128 S. Ct. 2733 (2008), is misplaced. The massive multi-layered settlement agreement at issue here is far removed from the prototypical long-term power contracts that were at issue in *Morgan Stanley*. While Petitioners sought panel rehearing and rehearing *en banc* of this matter before the D.C. Circuit Court, that court denied the rehearing petition, with no judges voting to rehear the case. Indeed, FERC itself has not asked this Court to hear the case. The petition should be denied.

I. STATUTORY BACKGROUND

Under Section 205 of the Federal Power Act, all rates filed with the Federal Energy Regulatory Commission must be "just and reasonable." 16 U.S.C. § 824d. Section 206 provides that "upon complaint" the FERC must determine whether a challenged rate is "unjust, unreasonable, unduly discriminatory or preferential." 16 U.S.C. § 824e.

Under the *Mobile-Sierra* doctrine, when sellers enter into freely negotiated wholesale energy contracts with purchasers, the Commission must presume that the negotiated rate is "just and reasonable." *See Morgan Stanley*, 128 S. Ct. at 2737; *see also* 16 U.S.C. §§ 824d, 824e. In wholesale markets, the buyer and seller are often "sophisticated businesses enjoying presumptively equal bargaining power, who could be expected to negotiate a 'just and reasonable' rate as between the two of them." *Verizon Commc'ns v. FCC*, 535 U.S. 467, 479 (2002).

In *Mobile* and *Sierra*, the Court recognized that buyers and sellers that have agreed to fix rates by contract do not have the right to seek to modify those rates by regulatory interdiction simply because it is in their private interest to do so. In *Mobile*, the Court held that a supplier does not have the right to change its rate contracts unilaterally by filing a new tariff schedule and that such a filing is a "nullity." *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332, 336 (1956). In *Sierra*, the Court held that a contract party asking a regulatory authority to

modify a contract rate must demonstrate that the existing rate is "so low as to adversely affect the public interest—as where it might impair the financial ability of the public utility to continue its service, cast upon other consumers an excessive burden, or be unduly discriminatory." *FPC v. Sierra Pacific Power Co.*, 350 U.S. 348, 355 (1956). The Court explained that:

> [W]hile it may be that the Commission may not normally impose upon a public utility a rate which would produce less than a fair return, it does not follow that the public utility may not itself agree by contract to a rate affording less than a fair return or that, if it does so, it is entitled to be relieved of its improvident bargain.

Id.

The Commission and the Courts of Appeals have referred to the much more restrictive mode of review under the *Mobile-Sierra* doctrine as the "public interest standard," as opposed to the ordinary "just and reasonable standard." *Morgan Stanley*, 128 S. Ct. at 2740 (citing *Southern Co. Servs., Inc. et al.*, 39 FERC ¶ 63,026 at PP 65,134, 65,141 (1987); *Kansas Cities v. FERC*, 723 F.2d 82, 87-88 (D.C. Cir. 1983); *Northeast Utils. Serv. Co. v. FERC*, 993 F.2d 937, 961 (1st Cir. 1993)). As this Court has observed, however, this "nomenclature" refers to the differing application of the just and reasonable standard to contract rates. *Id.* (citing *Philadelphia Elec. Co.*, 58 F.P.C. 88, 90 (1977)).

Although the public interest showing is the default mode of review of contract modifications sought by a contract party, this Court has held that parties to a contract can agree that the *Mobile-Sierra* presumption shall not apply. *See United Gas Pipe Line Co. v. Memphis Light, Gas & Water Div.*, 358 U.S. 103, 110-113 (1958). "[I]n the absence of any contractual relationship rates determined ex parte by the seller may be filed under § 4(d) [of the Natural Gas Act]. . . . We perceive no tenable basis of distinction between the filing of such a rate in the absence of contract and a similar filing under an agreement which explicitly permits it." *Id.* at 112-113 (internal citations omitted). Thus, the contract parties can agree that they may challenge the contract rate if it results in an unfair rate of return, not just if it violates the public interest. *See Morgan Stanley*, 128 S. Ct. at 2739 (citing *Papago Tribal Util. Auth. v. FERC*, 723 F.2d 950, 953, 955 (D.C. Cir. 1983); *Louisiana Power & Light Co. v. FERC*, 587 F.2d 671, 675-676 (5th Cir. 1979)). Such provisions are referred to as "*Memphis* clauses."

II. THE CONTESTED SETTLEMENT

This case arose from a highly contested FERC proceeding in which ISO New England, the independent system operator that manages the reliability of the bulk power system in New England, filed changes to its market rules tariff to address deficiencies in the mechanism for procuring generation capacity. Pet. App. 105a. After two years

of litigation, 107 parties reached a settlement; eight parties, including the respondents here, opposed the settlement. *Id.* at 110a. Thus, there was no agreement between the settling parties and the respondents. That settlement was subject to approval by the Commission.

The proposed settlement created a forward capacity market, in which annual auctions would determine the market clearing price of electric generation capacity three years in advance of when that capacity would be needed. *Id.* The auctions would procure the generating capacity required to satisfy the installed capacity requirement, which is the minimum level of capacity needed to maintain the reliability of the grid. *Id.* at 112a. Each utility serving end-use customers would be required to pay for a share of the installed capacity requirement, based on its proportional share of peak load. *Id.*

Because there would be a three-year gap between the first auction and the year that the capacity procured through the auction would be provided, the settling parties agreed upon a transition period, during which all qualifying generating capacity resources would receive fixed payments between December 1, 2006 and ending on June 1, 2010. *Id.* at 116a. The cost of these payments similarly would be allocated to utilities based on their proportionate share of peak load. *Id.* at 117a.

The settlement agreement contains a provision (§ 4.C) purporting to impose the *Mobile-Sierra*

presumption against challenges to the capacity clearing prices derived from the annual forward capacity auctions and challenges to the transition period payments, whether the challenge is made "by a Settling Party, a non-Settling Party, or the FERC acting *sua sponte*." *Id.* at 193a-194a (quoting § 4.C of the settlement agreement). The settlement agreement also contains a *Memphis* clause exempting all other terms of the settlement agreement from the operation of the *Mobile-Sierra* presumption. *Id.* at 194a.

FERC approved the *Mobile-Sierra* provision, noting that it has permitted the use of similar provisions in the past, citing a string of cases dating back to 2003. *Id.* at 200a-201a. FERC found the provision "reasonable" because FERC still retains authority to protect non-settling parties under the public interest mode of review, and because the settlement agreement permits parties to challenge ISO New England's "informational filings" on the auction results under the just and reasonable mode of review when ISO New England files them under section 205. *Id.* at 78a, 201a-202a. Finally, FERC concluded that it was appropriate to apply the *Mobile-Sierra* presumption to non-settling parties in order to achieve "contractual stability." *Id.* at 202a.

III. THE DECISION BELOW

In the decision below, the D.C. Circuit held that, in approving the settlement agreement, the Commission

unlawfully deprived non-settling parties—including the respondents—"of their statutory right" under the Federal Power Act "to challenge rates under the 'just and reasonable' standard." *Id.* at 19a. The court found that "[t]his case is clearly outside the scope of the *Mobile-Sierra* doctrine." *Id.* at 22a. The court stated that *Mobile-Sierra* is invoked when "one party to a rate contract on file with FERC attempts to effect a unilateral rate change by asking FERC to relieve its obligations under a contract whose terms are no longer favorable to that party." *Id.* (quoting *Maine PUC v. FERC*, 454 F.3d 278, 284 (D.C. Cir. 2006)). The court found that "the settling parties are attempting to thrust the 'public interest' standard of review upon non-settling third parties who have vociferously objected to the terms of the settlement agreement." *Id.* The court noted that "[i]t goes without saying that a contract cannot bind a nonparty." *Id.* (quoting *EEOC v. Waffle House, Inc.*, 534 U.S. 279 (2002). The court stated that the purpose of the *Mobile-Sierra* doctrine is to "preserve the terms of the bargain as between the contracting parties." *Id.* (citing *Atlantic City Elec. Co. v. FERC*, 295 F.3d 1, 14 (D.C. Cir. 2002). The court held that "when a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply; the proper standard of review remains the 'just and reasonable' standard in section 206 of the Federal Power Act." *Id.*

The court rejected FERC's justifications for the *Mobile-Sierra* provision, that the public interest

showing will only apply to future challenges to a narrow category of rates or that non-settling parties are adequately safeguarded under the Commission's retained authority under *Mobile-Sierra*, holding that approval of the agreement still deprives non-settling parties of their statutory right to have rate challenges adjudicated under the "just and reasonable" showing. *Id.* at 22a-23a. The court also rejected FERC's argument that the Commission has routinely approved contracts that apply the public interest review to non-contracting parties, noting that the Commission has only done so since 2002 and that none of the decisions to which FERC cited have been subject to judicial review on the *Mobile-Sierra* issue. *Id.* at 23a.

Finally, with respect to the need for contract stability, the court explained that "the *Mobile-Sierra* doctrine is designed to ensure contract stability *as between the contracting parties—i.e.*, to make it more difficult for either party to shirk its contractual obligations." *Id.* at 24a (citing *Atlantic City*, 295 F.3d at 14) (emphasis in original). The court observed that "[i]t makes no sense to say that the values of 'stability' and 'certainty' are furthered by applying the deferential standard of review to the eight parties that *refused* to agree to the terms of the settlement." *Id.* (emphasis in original).

Petitioners and FERC sought rehearing of the decision below after this Court issued its decision in *Morgan Stanley*. Two FERC commissioners dissented from FERC's decision to seek rehearing, arguing that

the decision below was consistent with *Morgan Stanley* and does not damage FERC's ability to approve settlements of contested proceedings before the Commission. Pet. App. 224a.

REASONS FOR DENYING THE PETITION

There are no compelling reasons to grant certiorari in this case. This case does not involve the sort of bilateral contract to which the *Mobile-Sierra* doctrine directly applies and with which the *Morgan Stanley* decision was concerned. To the contrary, this case involves a massive, contested settlement agreement regarding the overall structure of New England's power capacity market. It is undisputed that the 107 settling parties and the eight parties that opposed the settlement did not reach an agreement between them. Those opponents did not enter into any bargain, in exchange for any beneficial term of the settlement, to waive their right to challenge any yet-to-be-determined rates resulting from a newly established market mechanism except upon a showing of unequivocal public necessity. This is simply the wrong case through which to address "[w]hether *Mobile-Sierra's* public-interest standard applies when a contract rate is challenged by an entity that was not a party to the contract." Pet. (i).

Moreover, the decision below does not conflict with the decision of another court of appeals on the question presented or with *Morgan Stanley*. No court

of appeals has addressed a challenge to a wholesale power contract rate brought by a non-party to the contract—let alone addressed a challenge to a massive settlement agreement to create an entirely new and novel market structure brought by entities that opposed the agreement. And *Morgan Stanley* did not speak to the issue of non-party rights. The D.C. Circuit's well-reasoned decision does not merit this Court's review, as confirmed by FERC's decision not to seek this Court's review.

I. THE SETTLEMENT AGREEMENT DOES NOT FALL WITHIN THE *MOBILE-SIERRA* DOCTRINE

Certiorari should be denied because the facts and posture of this case make it an inappropriate vehicle to test the Petitioners' general question of whether the *Mobile-Sierra* doctrine applies to a challenge by *any* non-party to *any* ordinary wholesale power contract bilaterally agreed to by a seller and buyer. The "contract" that Petitioners seek to impose upon non-contracting third parties is fundamentally different from the privately negotiated bilateral energy contracts that were at issue in *Morgan Stanley*. The settlement agreement was not a privately negotiated contract, but rather "emanated from a highly contested adjudicatory proceeding before the Commission and involves a broad, public matter." Pet. App. 228a. Whereas the *Mobile-Sierra* doctrine assumes that "sophisticated businesses enjoying presumptively equal bargaining power . . .

could be expected to negotiate a 'just and reasonable' rate as between the two of them," *Verizon*, 535 U.S. at 479, "no 'commonsense notion' would hold that the 115 parties to the adjudication of this matter enjoy presumptively equal bargaining power." Pet. App. 228a (quoting FERC Commissioners Kelly and Wellinghoff); *cf. Morgan Stanley*, 128 S. Ct. at 2746.

Moreover, neither the settlement agreement nor the forward capacity market contemplated in the settlement agreement result in rates fixed by negotiated bilateral contracts between buyers and sellers. The settlement provisions for transition period payments and for payments under the forward capacity market were to be implemented through then yet-to-be-developed tariff revisions. *Id.* at 118a. In other words, the settling parties agreed that prices would be set by a tariff-based regulatory process. Although the settling parties certainly could agree amongst themselves that they could challenge the rates resulting from that process only upon a showing that the rates are contrary to the "public interest," the rates set by that tariff-based process remain subject to the ordinary "just and reasonable" mode of review.

Because this case does not present a situation where a bilateral wholesale contract is being challenged by a party or even a non-party to a bilateral wholesale contract, it is inappropriate to grant certiorari on the Petitioners' question in this case. Moreover, the situation here, where the Commission was asked to approve an entirely new

and novel market structure, is unlikely to recur frequently, and thus, the interest of justice does not require the Court to address whether the *Mobile-Sierra* doctrine applies in these circumstances.

II. THE DECISION BELOW DOES NOT CONFLICT WITH THE DECISION OF ANY OTHER UNITED STATES COURT OF APPEALS OR THIS COURT ON THE SAME MATTER

A. There is no Split Between the Courts of Appeals on this Issue

No court has previously addressed whether the *Mobile-Sierra* doctrine applies to a challenge to a contract rate brought by an entity that was not a party to the contract. This is why the D.C. Circuit in the decision below explicitly stated that "[i]n the instant case, we are presented with a question of first impression: may the Commission approve a settlement agreement that applies the highly-deferential public interest standard to rate challenges brought by non-contracting third parties?" Pet. App. 20a. Because the decision below is the first appellate decision addressing this issue, there is no compelling reason to grant the petition for a writ of certiorari. S. Ct. Rule 10(a).

Petitioners cite several cases that they claim support the proposition that courts have previously determined that the *Mobile-Sierra* doctrine "protects contract rates from all challenges—whether by

parties or non-parties, including FERC acting *sua sponte*." Pet. 26. Petitioners cite *Northeast Utils. Serv. Co. v. FERC*, 993 F.2d 937 (1st Cir. 1993), and *Boston Edison Co. v. FERC*, 233 F.3d 60 (1st Cir. 2000), for the proposition that "when FERC—which is not a contracting party—seeks to challenge a contract rate as unjust or unreasonable, FERC too must overcome the Mobile-Sierra presumption." Pet. 26. Petitioners draw the incorrect conclusion from these rulings. In both of those cases, the courts concluded that the FERC must apply the *Mobile-Sierra* presumption as between the parties to a bilateral contract.

Petitioners also cite *Boroughs of Chambersburg v. FERC*, 580 F.2d 573 (D.C. Cir. 1978), *Public Serv. Co. of Indiana, Inc. v. FERC*, 575 F.2d 1204 (7th Cir. 1978), *Town of Norwood v. FERC*, 587 F.2d 1306 (D.C. Cir. 1978), and *Wisconsin Public Power v. FERC*, 493 F.3d 239 (D.C. Cir. 2007), for the proposition that "courts have repeatedly invoked *Mobile-Sierra* to reject the efforts of non-parties to invalidate (as discriminatory or unjust) the contracts of others." Pet. 27-28. These cases also do not stand for the proposition for which they are cited.

As Petitioners acknowledge, these cases involved claims of "undue discrimination" and the question of whether disparities between *Mobile-Sierra* contract rates and rates made available to other non-contracting customers constitute prohibited discrimination. Thus, the decisions in these cases addressed challenges to existing contracts, not on the grounds that the contracts would bind the third-party

challengers, but instead upon the grounds that contract counterparties received more favorable terms and conditions of service than those provided to other non-contracting third parties. *See, e.g.*, *Wisconsin Public Power*, 493 F.3d at 269-275. Unlike here, the contracts in question in the cases upon which Petitioners rely did not purport to bind third parties to take service under their privately negotiated terms and conditions. Nor did those contracts and the *Mobile-Sierra* protections afforded their parties purport to deprive any third party of its statutory right to challenge any rate applicable to the third party under the ordinary just and reasonable review.

The remaining cases cited by Petitioners also do not address the issue of applying the *Mobile-Sierra* presumption to non-contracting third parties. For example, Petitioners cite to *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 767 (1968), for the proposition that because "the regulatory system created by the Act is premised on contractual agreements voluntarily devised by the regulated companies[,] it contemplates abrogation of these agreements only in circumstances of unequivocal public interest." Pet. 17. While this is true where, as in *Permian Basin*, the Court was enforcing the terms of a contract as between the counterparties to that contract, it is absolutely irrelevant in the instant case. *Permian Basin* does not stand for the proposition that the same level of review should be applied to challenges by non-contracting third parties,

particularly where, as here, the non-contracting third parties would be bound to the contract by force of a settlement agreement to which they objected.

B. Neither *Morgan Stanley* Nor Any Other Decision by this Court Stands for the Proposition That *Mobile-Sierra* Should Apply to Challenges by Non-Signatories to a Settlement Agreement

The D.C. Circuit's decision in no way conflicts with this Court's decision in *Morgan Stanley*. In *Morgan Stanley*, this Court stated that the premise behind the *Mobile-Sierra* doctrine "was grounded in the commonsense notion that '[i]n wholesale markets, the party charging the rate and the party charged [are] often sophisticated businesses enjoying presumptively equal bargaining power, who could be expected to negotiate a 'just and reasonable' rate *as between the two of them*.'" *Morgan Stanley*, 128 S. Ct. 2733, 2740 (citing *Verizon*, 535 U.S. 467) (emphasis added). This Court reasoned that "when commercial parties . . . avail themselves of rate agreements, the principal regulatory responsibility [is] not to relieve a contracting party of an unreasonable rate." *Id.* Such a policy would serve to undermine the important role that contracts serve in promoting market stability. As the Court made clear:

> [b]y enabling sophisticated parties who weathered market turmoil by entering long-term contracts to renounce those contracts once the storm has passed, the

> Ninth Circuit's holding would reduce the incentive to conclude such contracts in the future. Such a rule has no support in our case law and plainly undermines the role of contracts in the FPA's statutory scheme.

Morgan Stanley, 128 S. Ct. at 2747.

Contrary to Petitioners' claim, the point in *Morgan Stanley* is that the contracting parties are bound to their agreement; it does not impose the *Mobile-Sierra* doctrine upon those who did not enter into the contract. While the Court made clear that FERC's regulatory responsibility is not to "relieve a contracting party of an unreasonable rate," *Morgan Stanley*, 128 S. Ct. at 2740, that in no way suggests that the FERC may impose that same improvident rate upon a non-contracting third party, who has never agreed to the terms of the settlement and received no concessions in exchange for which the parties traded away their rights to seek review of rates under the ordinary just and reasonable showing.

In its ruling below, the D.C. Circuit correctly applied precisely the same reasoning articulated by this Court. The D.C. Circuit stated that, "[i]n *Mobile*, the Supreme Court stated that 'the relations *between the parties*' may be established by contract, subject only to the 'public interest' review." Pet. App. 21a (citing *Mobile*, 350 U.S. at 339) (emphasis in the original)). It concluded that applying the *Mobile-Sierra* presumption was "premised on the existence of a voluntary contract between the parties." Pet. App.

21a. The D.C. Circuit stated that the "purpose of the *Mobile-Sierra* doctrine is 'to preserve the benefits of the *parties' bargain* as reflected in the *contract*, assuming that there was no reason to question what transpired at the contract formation stage.'" Pet. App. 21a (quoting *Atlantic City Elec. Co. v. FERC*, 295 F.3d 1, 14 (D.C. Cir. 2002)) (emphasis added)).

In the instant case, there is no valid contract between the eight non-settling parties and the 107 signatories to the contested settlement agreement in the underlying Commission proceeding. There can be no assumption that those non-settling parties had negotiated a just and reasonable rate or indeed had negotiated any benefits for themselves—the very assumption that is the precondition for the application of the *Mobile-Sierra* doctrine.

III. THERE IS NO COMPELLING REASON FOR THIS COURT TO REVIEW WHETHER THE *MOBILE-SIERRA* DOCTRINE SHOULD APPLY TO NON-CONTRACTING PARTIES IN THIS CASE

A. The Decision Below Was Correctly Decided

Petitioners argue that the decision below "conflicts with decades of settled practice." Pet. 25. They further argue that the court of appeals misunderstood or misapplied the standard of review and that the court mistakenly relied on contract law to support its determination that the *Mobile-Sierra*

doctrine does not extend to parties that contested a settlement agreement. As discussed below, however, Petitioners fail to recognize that (1) FERC does not have any long-standing practice of applying the *Mobile-Sierra* doctrine to third parties, (2) the decision below applied the correct standard of review and is consistent with FERC practice relating to approval of contested settlements, and (3) the court properly relied on contract principles in refusing to apply the *Mobile-Sierra* doctrine to non-settling third parties.

The FERC policy of applying the *Mobile-Sierra* presumption to non-contracting third parties is not a "longstanding position." Pet. 12. To the contrary, as the FERC acknowledged to the D.C. Circuit, this policy dates back only as far as 2002. Pet. App. 23a. Petitioners fail to acknowledge this position's recent vintage and make no effort to reconcile FERC's pre-2002 *Mobile-Sierra* policy with their sweeping declaration that the D.C. Circuit decision "conflicts with decades" of practice. That is because they cannot. In fact, FERC's approval of the *Mobile-Sierra* presumption to non-contracting parties, as in the underlying proceeding, is a recent innovation that has never been subject to judicial review.

Until 2002, FERC expressly refused to apply the *Mobile-Sierra* presumption to third parties. For example, in *PJM Interconnection*, 96 FERC ¶ 61,206 at P 61,878 (2001), FERC rejected an argument that parties to a contract may "bind not only one another, but also other entities who are not parties to that

contract (and did not receive the contractual benefits in exchange for which the parties traded away their right to seek rate changes)." Thus, the D.C. Circuit's decision below is not a new rule, but rather is in keeping with FERC's rationale prior to 2002.

Even after 2002, FERC continued to reject agreements that applied the *Mobile-Sierra* presumption to non-signatories in contested settlement agreements. *See, e.g., Milford Power Company, LLC*, 119 FERC ¶ 61,167, at P 31 (2007); *Bridgeport Energy, LLC*, 118 FERC ¶ 61,243 at P 41 (2007). Just as in the instant case, FERC observed that the purpose of certain types of agreements with generators to provide reliability service have a "wide applicability" to market participants that are much broader in number than the entities executing the agreements. *Id.* In these cases, FERC determined that it was inconsistent with its duty under the Federal Power Act to be bound to the restrictive public interest mode of review when reviewing such agreements. FERC determined that "any challenges to the . . . agreement by non-parties under section 206 of the FPA shall be reviewed by the Commission under the just and reasonable standard." *Milford Power*, 119 FERC ¶ 61,167, at P 31; *see also Bridgeport Energy*, 118 FERC ¶ 61,243 at P 41 (2007).

Petitioners argue that the D.C. Circuit erred in rejecting the "application of *Mobile-Sierra* to non-party challenges because it would 'deprive th[ose non-parties] of their statutory right to challenge rates under the 'just and reasonable' standard.'" Pet. 23. Petitioners

state that this Court's decision in *Morgan Stanley* "held that there 'is only one statutory standard for assessing wholesale electricity rates, whether set by contract or tariff—the just and reasonable standard.'" Pet. 24 (citing *Morgan Stanley*, 128 S. Ct. at 2745). They claim that the decision below was in error, because the Court in *Morgan Stanley* rejected the view that *Mobile-Sierra* departs from the statutory just and reasonable standard. *Id.*

The Petitioners read too much into the D.C. Circuit's references to the "just and reasonable" and "public interest" standards. In *Morgan Stanley*, this Court observed that the Commission and the Courts of Appeals have used this longstanding nomenclature to refer to the two modes of review under the single, statutory "just and reasonable" standard. *Morgan Stanley*, 128 S. Ct. at 2740. There is nothing in the D.C. Circuit's decision below to suggest that the court misunderstood or intended to modify the standard of review.

The D.C. Circuit did not base its decision on whether the *Mobile-Sierra* presumption was either an extra-statutory standard or an application of the "just and reasonable standard in the contract context." Instead, the court correctly determined that the *Mobile-Sierra* presumption only applies when there is a voluntary contract among the parties and not, as here, when there were "non-settling third parties who have vociferously objected to the terms of the settlement agreement." Pet. App. 22a. The court concluded that "it goes without saying that a contract

cannot bind a nonparty." *Id.* (citing *EEOC v. Waffle House, Inc.*, 534 U.S. 279, 294 (2002)).

The policy concerns present in *Morgan Stanley* are not present here. In *Morgan Stanley*, the buyers had "buyer's remorse" after the crisis in the California markets had passed. *Morgan Stanley*, 128 S. Ct. at 2743. The Court was concerned that, in such circumstances, "enabling sophisticated parties who weathered market turmoil by entering long-term contracts to renounce these contracts once the storm has passed . . . would reduce the incentive to conclude such contracts in the future." *Id.* at 2747.

The circumstances in the present case are far different. Respondents do not have buyer's remorse, because they never agreed to the terms of the settlement agreement. FERC can still apply the *Mobile-Sierra* presumption to challenges raised by any of the signatories to the settlement agreement, which would promote contract stability. Applying the *Mobile-Sierra* presumption to rate challenges raised by non-settling parties, on the other hand, could promote uncertainty in energy markets and promote gaming of settlement proceedings, undermining the very market stability that Petitioners claim is essential to industry stability. As Commissioners Kelly and Wellinghoff argued:

> The agreement . . . is a settlement of an adjudication that 107 of 115 parties to the proceeding signed. If the *Mobile-Sierra* standard is applied to this settlement, what does it mean for future settlements? Would it

> apply to any settlement arrived at by the utility with any of the intervening parties? What if the utility achieved the agreement of one party out of 115? How about 50 parties out of 115? How about two parties out of seven? What if the two settling parties were affiliates of the utility? . . . The gaming scenarios this could spawn are countless. The uncertainty would be boundless.

Pet. App. 231a-232a. Applying the *Mobile-Sierra* presumption to non-settling parties would lead to the absurd result that two parties in a complex, multiparty proceeding could settle amongst themselves to fix rates or a mechanism to fix rates and bind all other non-settling parties to take or offer service at those rates absent a showing that the agreement unequivocally harms the public interest.

Applying the *Mobile-Sierra* presumption to non-contracting third parties would create an extraordinary modification of the rights of non-settling parties in contested settlements. This is because, as this Court made clear, the *Mobile-Sierra* presumption applies at every level of review of the contract, including at the FERC's initial review of whether to approve the settlement agreement in the first place. In *Morgan Stanley*, this Court flatly rejected the Ninth Circuit's determination that "all initially filed contracts must be subject to review without the *Mobile-Sierra* presumption," ruling instead that the presumption of reasonableness

would apply "regardless of when the contract is reviewed." *Morgan Stanley*, 128 S. Ct. at 2746.

Petitioners explain that this case involves a "disagreement over the standard that would govern *future* challenges" to transition rates or rates that result from the auction process, but maintain that the case "does not concern the standard FERC applied in this case when deciding whether to approve the settlement agreement itself." Pet. 7 (emphasis in original). However, they fail to acknowledge the potentially far-reaching effect of expanding the *Morgan Stanley* holding to apply to non-settling parties.

Since, as discussed above, under *Morgan Stanley*, FERC must presume that a bilateral wholesale contract is just and reasonable as between the parties to the contract, expanding this holding to apply the *Mobile-Sierra* doctrine to parties contesting a settlement brings into question the standard that the Commission is to apply to contested settlements. Currently, when a utility files a tariff change under section 205, the Commission reviews whether it is just and reasonable. Petitioners' invitation to expand *Morgan Stanley's* holding could disturb the Commission's existing ability to determine the reasonableness of contested settlement agreements and would result in significant decision-making authority being transferred from the Commission to the utility and other private parties entering into the settlement agreement. As Commissioners Kelly and Wellinghoff stated in their dissent to the

Commission's decision to request rehearing of the *Mobile-Sierra* portion of the decision below, allowing the Commission to hold a settlement agreement to any standard other than the "ordinary" just and reasonable standard "would cause untold uncertainty in future adjudications before the Commission; would be unduly discriminatory to applicants for tariff changes who do not obtain settlement agreements; and would result in a regulatory morass of utility tariff provisions with differing status." Pet. App. 230a.

Finally, Petitioners' effort to argue that principles of contract law weigh against the decision below is inconsistent with *Mobile-Sierra* precedent. Petitioners take issue with the D.C. Circuit's citation to *EEOC v. Waffle House, Inc.*, 534 U.S. 279 (2002) ("[i]t goes without saying that a contract cannot bind a nonparty."). First, they state "the premise that *Mobile-Sierra* derives from, and is bounded in scope by, contract law is incorrect." Pet. App. 22a. However, Petitioners ignore that the very rationale for *Mobile-Sierra* is rooted in the basic constructs of contract law. As stated in the decision below, "[i]n *Mobile*, the Supreme Court stated that 'the relations *between the parties*' may be established by contract, subject only to the 'public interest' review." Pet. App. 21a (citing *United Gas Pipeline Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332, 339 (1956)). Petitioners' argument is also inconsistent with the Court's reliance on the role of contract principles in the development of the *Mobile-Sierra* doctrine. As the

Court stated in *Morgan Stanley*, "[b]y enabling sophisticated parties who weathered market turmoil by entering long-term contracts to renounce those contracts once the storm has passed, the Ninth Circuit's holding would reduce the incentive to conclude such contracts in the future. Such a rule has no support in our case law and plainly undermines the role of contracts in the FPA's statutory scheme." *Morgan Stanley*, 128 S. Ct. at 2147. Thus, the fact that *Mobile-Sierra* "comes from the FPA," Pet. 30, says nothing about the incorporation of contract principles into the doctrine. In fact, it is clear that at its core, the application of *Mobile-Sierra* requires a "voluntary contract between the parties." Pet. App. 21a.

Second, Petitioners rely on *Local No. 93 Int'l Ass'n of Firefighters v. City of Cleveland*, 478 U.S. 501 (1986), to argue that application of *Mobile-Sierra* to non-settling parties does not "bind" them and therefore is not inconsistent with contract law. Petitioners argue, relying on *Firefighters*, that application of the *Mobile-Sierra* doctrine to future rate challenges by non-settling parties does not impose any legal duties on non-settling parties or resolve any claims they may have.

Contrary to Petitioners' claims, *Firefighters* does not stand for the proposition for which it was cited. In *Firefighters*, the issue was whether a non-settling party's agreement was required before a district court could approve the consent decree at issue. The Court held that agreement was not required because the

consent decree *would not affect the non-settling party's rights*. 478 U.S. at 529-30. Of course, in the present case, application of the *Mobile-Sierra* doctrine to non-settling parties would require non-settling parties to make the stringent public interest showing in future rate challenges to transition payments or auction prices resulting from the settlement agreement. Thus, the application of the *Mobile-Sierra* doctrine to non-settling parties would affect their statutory rights under the FPA.

B. The Decision Below Will Not Threaten Industry Stability

Petitioners' claim that the decision below will threaten industry stability is without merit and should be rejected. *See* Pet. 19-23. Petitioners argue that the decision will open the door to "any one of that boundless group of non-parties and potential surrogates [to] ask[ ] FERC to abrogate a contract." *Id.* at 19. The Petitioners claim, therefore, that the "'third party exception' to *Mobile-Sierra's* public interest standard will engulf the rule and destroy the stability it is designed to provide." *Id.*

As discussed, *supra*, FERC previously took the position that the *Mobile-Sierra* doctrine should not be applied to non-contracting parties. Yet, this posed no threat to industry stability. Even under the ordinary just and reasonable review, an entity with standing to challenge a utility's tariff provision must prove that circumstances have changed so dramatically that the

tariff provision has become unjust and unreasonable. Overcoming this substantial obstacle "does not happen often." Pet. App. 238a (dissent of Commissioners Kelly and Wellinghoff (Aug. 4, 2008)).

Finally, contrary to Petitioners' claims, the D.C. Circuit's decision below will not occasion the collapse of the electricity infrastructure in New England. As the D.C. Circuit explained, the *Mobile-Sierra* presumption of reasonableness ensures contract stability "*as between the contracting parties*" and "[i]t makes no sense to say that the values of 'stability' and 'certainty' are furthered by applying the deferential standard of review to the eight parties that *refused* to agree to the terms of the settlement." *Id.* at 24a (emphasis in original). If settling parties cannot legally bind non-settling parties to their agreement, they may choose to compromise other aspects of the settlement with the non-settling parties in order to obtain their agreement to limit their rights under Section 206. Alternatively, to the extent that the settling parties value those other aspects of the settlement greater than absolute certainty, they may choose to settle amongst themselves without that certainty. There is no need for the Court to address whether the *Mobile-Sierra* doctrine should apply in this case, because the settling parties remain free to choose whether to reach a settlement with all parties.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

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REPLY BRIEF

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IN THE

Supreme Court of the United States

NRG POWER MARKETING, LLC, *ET AL.*,
Petitioners,

v.

MAINE PUBLIC UTILITIES COMMISSION, *ET AL.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

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CORPORATE DISCLOSURE STATEMENT

Pursuant to Supreme Court Rule 29.6, petitioners NRG Power Marketing, LLC, Devon Power LLC, Connecticut Jet Power LLC, Norwalk Power LLC, Middletown Power LLC, Montville Power LLC, and Somerset Power LLC state that the corporate disclosure statement included in the petition remains accurate.

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REPLY FOR PETITIONERS

For more than 50 years, *Mobile-Sierra* has protected the "stability of supply arrangements" that is "essential to the health of the [energy] industry." *United Gas Pipe Line Co.* v. *Mobile Gas Serv. Corp.*, 350 U.S. 332, 344 (1956). Under *Mobile-Sierra*, FERC must "presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement," and FERC cannot abrogate such a rate except "'in circumstances of unequivocal public necessity.'" *Morgan Stanley Capital Group Inc.* v. *Pub. Util. Dist. No. 1*, 128 S. Ct. 2733, 2737, 2739 (2008) (quoting *Permian Basin Area Rate Cases*, 390 U.S. 747, 822 (1968)).

The decision below guts that protection. Under it, the *Mobile-Sierra* presumption applies *only* to challenges brought by the contracting parties themselves. Literally anyone else—any consumer, advocacy group, utility commission, or state attorney general—can challenge contract rates free from *Mobile-Sierra*. Recognizing the decision's impact, FERC urged below that this case "presents a question of *exceptional importance*" because it "undermines the contract certainty needed for infrastructure investment." FERC Pet. for Reh'g and Reh'g En Banc, Nos. 06-1403, *et al.*, at 10, 12 (D.C. Cir. Aug. 8, 2008) (emphasis added). The decision, FERC added, is "manifestly anomalous" and "misapprehen[ds]" the law. *Id.* at 5, 11.

Before this Court, FERC characterizes the decision below as "anomalous" and urges the Court to grant the petition, vacate, and remand in light of this Court's intervening decision in *Morgan Stanley*. FERC Br. 11, 12-14. Seeking to forestall plenary review, however, FERC downplays the decision's importance, urging that "ordinary" just-and-reasonable review is adequately protective. But that argument is impossible to reconcile with

Mobile-Sierra and *Morgan Stanley*. And FERC's own actions following the D.C. Circuit's decision underscore the need for review.

I. THE DECISION BELOW PRESENTS AN ISSUE OF EXCEPTIONAL IMPORTANCE

A. Despite having urged below that the court of appeals' decision has "exceptional importance"—sufficient importance to warrant FERC's first petition for rehearing *en banc* in almost five years, see FERC Reh'g Pet. 2 & n.2, 10—FERC now asserts that the decision is perhaps not so important after all. *Mobile-Sierra*'s protection can be jettisoned, FERC urges, because "the ordinary just-and-reasonable standard would itself furnish substantial protection." FERC Br. 10-11. But that is precisely the argument FERC made in opposing review in *Morgan Stanley*, see FERC Br. in Opp. in Nos. 06-1454, *et al.*, at 11-12, 17-18—and which this Court rejected on the merits.

Under the ordinary just-and-reasonable standard, FERC can modify rates whenever they deviate from an ill-defined "'zone of reasonableness.'" FERC Br. 10 (quoting *Permian Basin*, 390 U.S. at 767). *Mobile-Sierra*'s "public-interest" standard, by contrast, permits abrogation of contract rates "'only in circumstances of unequivocal public necessity'"—*i.e.*, "extraordinary circumstances where the public will be severely harmed." *Morgan Stanley*, 128 S. Ct. at 2739, 2749 (quoting *Permian Basin*, 390 U.S. at 822). As the court below recognized, "the public interest standard is 'much more restrictive' than the just and reasonable standard." Pet. App. 19a.

For precisely that reason, *Morgan Stanley* rejected the Ninth Circuit's substitution of a "zone of reasonableness" test for *Mobile-Sierra*'s public-interest standard. That ordinary just-and-reasonable formula, this Court

held, "fails to accord an adequate level of protection to contracts" and "give[s] short shrift" to their important role. 128 S. Ct. at 2747, 2749. Such a permissive standard "threaten[s] to inject more volatility into the electricity market by undermining a key source of stability." *Id.* at 2749. Yet FERC champions that same "'zone of reasonableness'" standard here. FERC Br. 10.

FERC stresses that ordinary just-and-reasonable review "gives the Commission *discretion* to take into account the facts and circumstances" and that "the Commission *may* take into account * * * the importance" of contract stability. FERC Br. 10-11 (emphasis added). But that is exactly the problem. *Mobile-Sierra* does not promote contract stability by granting FERC *discretion* to respect contracts when FERC deems it expedient. *Mobile-Sierra* promotes that goal by *denying* FERC discretion to modify contracts absent "unequivocal public necessity." *Morgan Stanley*, 128 S. Ct. at 2739, 2745. Energy companies cannot rationally invest hundreds of millions of dollars developing new infrastructure based on a regulator's assurance that it *might* consider contractual expectations when consumers, elected officials, or other non-parties later challenge contract rates. FERC's assurances that it "generally" examines reasonableness over a contract's life and "typically" requires a showing of changed circumstances (Br. 11) only underscore the malleability of its proposed standard. Mere "changed circumstances" are insufficient to meet *Mobile-Sierra*: The respondents in *Morgan Stanley* claimed changed circumstances, but this Court held that FERC "was *required* * * * to apply the *Mobile-Sierra* presumption" nonetheless. See 128 S. Ct. at 2743, 2745.

The non-federal respondents' assertion that the ordinary just-and-reasonable standard is a "substantial obstacle" to abrogation (Br. in Opp. 26-27) fails for the same reason. The vigor with which they challenge *Mobile-*

Sierra's applicability here belies their claim. The difference between the two standards was important enough to justify review—and reversal—in *Morgan Stanley*. It is no less important here.

B. FERC does not dispute that, because contract rates indirectly affect a vast array of consumers, regulators, and interest groups, the decision below creates a virtually unbounded class of potential complainants who can challenge contract rates free from *Mobile-Sierra*'s requirements. Under broad principles of administrative-law standing, *any person* claiming to be adversely affected can file a complaint challenging a rate. See 16 U.S.C. § 824e(a); 18 C.F.R. § 385.206(a); *United States* v. *SCRAP*, 412 U.S. 669, 689 n.14 (1973). Indeed, respondents nowhere dispute that, under the D.C. Circuit's theory, *Morgan Stanley* itself should have been resolved differently because one respondent there—the Nevada Attorney General, Bureau of Consumer Protection—was not a contracting party. See Pet. 21.

FERC suggests that it can mitigate the problem by weeding out challenges filed by a "proxy for one of the contracting parties." FERC Br. 11-12. But FERC does not explain what it means by a "proxy." It nowhere explains how a "proxy" exception would provide adequate protection unless that term encompasses every consumer, advocacy group, or state agency or official who might file an after-the-fact challenge. The decision below drew no distinction between proxies and other third parties. FERC never identifies the source of its authority to create a proxy exception for unrelated entities. Nor does FERC explain how such an exception can be administered without side-show trials exploring the relationships among various entities.

Declining to endorse FERC's proxy theory, the non-federal respondents urge that suppliers should "reach a settlement with all parties." Br. in Opp. 27. But the

court of appeals held that *any* non-contracting party can challenge an agreed-upon rate, not just settlement objectors. See Pet. App. 22a. And *Mobile-Sierra*'s promise of contract stability will be empty if it exists only where an energy supplier manages to contract with every *existing* and *future* person or entity that might someday be adversely affected by a contract rate.[1]

C. The decision below has mired the energy industry in uncertainty. Following the D.C. Circuit's decision, FERC has regularly required agreements submitted for filing—whether they be ordinary contracts or settlements, bilateral or multilateral, contested or uncontested—to replace any clause providing *Mobile-Sierra* protection with a clause that allows non-parties to challenge rates under the "most stringent standard permissible under applicable law." See App., *infra*, 1a-10a (listing scores of proceedings); Pet. 22 & n.8; *e.g.*, *Duke Energy Carolinas, LLC*, 123 FERC ¶61,201 at P10 & n.10 (2008). But no one knows what that standard means. And two of FERC's four active Commissioners have maintained—in more than 30 different opinions—that the D.C. Circuit's decision exempting non-party challenges from *Mobile-Sierra* "applies with at least equal force" to challenges by FERC itself. *E.g.*, *Devon Power LLC*, 126 FERC ¶61,027 (2009) (Kelly & Wellinghoff, Comm'rs, writing separately). *Mobile-Sierra* offers no promise of contract stability where so many can so readily deny that it applies to their challenges.

II. THIS CASE SQUARELY PRESENTS THE ISSUE

Unable to obscure the importance of the question presented, the non-federal respondents—but not FERC—claim this case is an unsuitable vehicle because it involves

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[1] APPA claims (Br. 23-26) that non-party challenges were infrequent in the past. But now that the D.C. Circuit has provided a roadmap for evading *Mobile-Sierra*, past experience is no guide.

a multiparty settlement agreement rather than an "ordinary wholesale power contract bilaterally agreed to by a seller and buyer." Br. in Opp. 10-12. That contention is triply mistaken.

First, the decision below drew no distinction between multiparty settlements and "ordinary wholesale power contract[s]." The court held categorically that, "when a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine *simply does not apply*." Pet. App. 22a (emphasis added). The correctness of that holding is the only question presented, and this case is an appropriate vehicle for addressing it.

Second, the distinction makes no sense. Settlement agreements *are* a species of contract. See *Kokkonen* v. *Guardian Life Ins. Co. of Am.*, 511 U.S. 375, 381 (1994). That an agreement is reached during litigation does not diminish its importance or reasonableness. Nor is there any basis in law or logic for distinguishing multiparty from bilateral contracts.

Finally, the proposed distinction does not even apply here. Petitioners do not claim that the *settlement agreement itself* should have been reviewed under *Mobile-Sierra*'s public-interest standard. The settlement in fact was reviewed under the ordinary just-and-reasonable standard, see Pet. App. 140a-144a, 200a, as the parties contemplated, see *id.* at 193a-194a. The question presented is whether *future* challenges will be subject to *Mobile-Sierra* in the two circumstances specified by the agreement: challenges to prices set at upcoming forward-capacity *auctions* (once FERC initially approves those prices), and challenges to transition payments. See *id.* at 6a, 193a-194a, 200a-203a.

Rates agreed upon through forward-capacity auctions are not meaningfully different from the "ordinary wholesale power contract[s]" respondents envision. Through

the auction, a willing utility commits to buy, and a willing supplier commits to sell, capacity at a particular price. See Pet. App. 110a-111a. That is the classic context—a voluntary agreement between sophisticated parties—where *Mobile-Sierra* has long applied. Those agreements, moreover, will often require suppliers to build new infrastructure. See *id.* at 110a. Yet the decision below would deny them *Mobile-Sierra* protection—potentially years into the contract, after the supplier has invested millions of dollars—if the challenge is brought by *anyone* other than a contracting party.[2]

III. THE DECISION BELOW IS INCORRECT AND INCONSISTENT WITH PRECEDENT

A. FERC neither defends the decision below nor retreats from its position that it is "manifestly anomalous" and a "misapprehension of [the] law." FERC Reh'g Pet. 5, 11; see also FERC Br. 11. Attempting a merits defense, the non-federal respondents urge that *Mobile-Sierra* does not apply here because, under general contract-law principles, contracts do not bind non-parties. Br. in Opp. 20-21, 24-26 (citing *EEOC* v. *Waffle House, Inc.*, 534 U.S. 279 (2002)). But respondents ignore the obvious flaw in that theory: Under general contract-law principles, *non-parties ordinarily cannot challenge a contract at all*, even if it indirectly affects them. See Pet. 31. Contract law gives shoppers no right to challenge the rate the local grocer agrees to pay a farmer for lettuce.

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[2] Because auction results are paradigmatic "ordinary wholesale power contract[s]," this case is an ideal vehicle (and it would not be necessary to resolve the status of transition payments, which could be addressed on remand and which terminate in May 2010 in any event, see Pet. App. 116a). The standard applicable to auction prices—and to all the wholesale contracts the decision below imperils—will continue to have great forward-looking importance until this Court resolves the issue.

The FPA departs from that contract-law norm by authorizing non-parties to challenge contract rates so long as they have standing under broad administrative-law principles. See p. 4, *supra*. But one cannot invoke general contract-law principles to *expand* a non-party's ability to challenge a rate where those contract-law principles would not permit him to challenge the rate *at all*.

In any event, *Mobile-Sierra* does not rest on the notion that contracting parties implicitly sign away their statutory rights. Rather, it reflects the sound principle that sophisticated buyers and sellers are likely to negotiate prices that are efficient and therefore presumptively "just and reasonable." That is why the doctrine is a constraint on *FERC's* authority to modify contracts rather than on the *contracting parties'* authority to challenge them. See Pet. 29-30. As this Court declared in the first sentence of its opinion in *Morgan Stanley*: "Under the *Mobile-Sierra* doctrine, the Federal Energy Regulatory Commission * * * must presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law." 128 S. Ct. at 2737. "That presumption would not necessarily cease to apply simply because the challenge to the rate came from a non-contracting party." FERC Br. 14.[3]

Burdens on third parties are certainly relevant to whether a challenge *satisfies Mobile-Sierra*'s public-

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[3] To support their claim that *Mobile-Sierra* does not apply to third-party challenges, respondents invoke *Morgan Stanley*'s observation that a sophisticated buyer and seller in a wholesale market can "be expected to negotiate a 'just and reasonable' rate *as between the two of them*." Br. in Opp. 15 (quoting 128 S. Ct. at 2740) (emphasis added by respondents). But that language merely explains *why* contract rates are presumed reasonable. The Court was not undermining its core holding that the rates are presumed reasonable, much less suggesting that the presumption may evaporate based on the challenger's identity.

interest standard. That standard permits FERC to consider, for example, whether a rate "cast[s] upon other consumers an excessive burden." *FPC* v. *Sierra Pac. Power Co.*, 350 U.S. 348, 354-355 (1956). The very fact that *Mobile-Sierra* contemplates evaluation of third-party harms, however, confirms that it covers *all* challenges to contract rates, including third-party challenges. See Pet. 28-29.

B. Courts have repeatedly applied *Mobile-Sierra* to third-party challenges. See Pet. 25-28. FERC argues that all but one of those cases involved "Commission-initiated investigation[s]" in which non-parties "raised arguments," not proceedings initiated by "third-party complaints." FERC Br. 8. But that distinction makes no sense. If *Mobile-Sierra* applied only when contracting parties challenge their own agreements, there would be no reason to apply that doctrine where FERC (itself a non-party) challenges a contract to vindicate third-party interests—whether FERC does so in a proceeding it initiates or following a third-party complaint. Tellingly, in FERC's order on remand in this case, two Commissioners expressly rejected the distinction FERC now invokes, urging that the D.C. Circuit's decision exempting third-party challenges from *Mobile-Sierra* "applies with at least equal force" to Commission challenges brought *sua sponte*. See p. 5, *supra*.

Northeastern Utilities Service Co. v. *FERC*, 993 F.2d 937 (1st Cir. 1993) ("*NUSCO*"), demonstrates the futility of respondents' effort to reconcile the cases. There, FERC modified an uncontested three-party contract *sua sponte* to require just and-reasonable review in future challenges, hypothesizing the agreement "might unduly discriminate against *entities not parties to the contract*." *Id.* at 960, 961 (emphasis added). The First Circuit held that concern "inadequate" to justify departure from *Mobile-Sierra* because "[t]he *Mobile-Sierra* doctrine itself

allows for intervention by FERC where it is shown that the interests of third parties are threatened." *Id.* at 961. The court later upheld FERC's subsequent order only because FERC "applied the 'public interest' doctrine on remand." *Ne. Utils. Serv. Co.* v. *FERC*, 55 F.3d 686, 692 (1st Cir. 1995). That decision, and others like it (Pet. 25-28), are impossible to square with the notion that non-party challenges are exempt from *Mobile-Sierra*.[4]

IV. At a Minimum, The Court Should Grant, Vacate, And Remand

Because the D.C. Circuit's decision eviscerates *Mobile-Sierra*, plenary review is warranted. At a minimum, the Court should grant, vacate, and remand in light of *Morgan Stanley*, as FERC suggests. FERC Br. 12-14.

As the petition explains (Pet. 23-25), the decision below conflicts with *Morgan Stanley* in at least two respects. First, the court of appeals erroneously treated *Mobile-Sierra* as "carv[ing] out an exception" to the statutory just-and-reasonable standard. Pet. App. 20a. That error was not a mere semantic misstep. Br. in Opp. 20-21. The court expressly based its holding on concerns about "depriv[ing] [non-]parties of their *statutory right*" to just-and-reasonable review. Pet. App. 22a-23a (emphasis added). *Morgan Stanley* makes clear that any such concern is unfounded because public-interest review under *Mobile-Sierra* is merely one *application* of the

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[4] Cases like *NUSCO* also answer the claim that FERC has applied *Mobile-Sierra* to third-party claims only since 2002. Br. in Opp. 18-19. To the extent FERC has episodically sought to narrow *Mobile-Sierra*—a doctrine it sometimes "very much dislikes," *Borough of Lansdale* v. *FPC*, 494 F.2d 1104, 1110 & n.28 (D.C. Cir. 1974) (citing cases)—cases like *NUSCO* have ensured that such flirtations are short-lived. Besides, any intermittent tergiversation at FERC underscores precisely why FERC must be *required* to follow *Mobile-Sierra* and the issue cannot be left to agency discretion.

statutory just-and-reasonable standard. 128 S. Ct. at 2740.

Second, the court of appeals' decision rests on the misperception that *Mobile-Sierra* seeks only "to make it more difficult for either *party* to shirk its contractual obligations." Pet. App. 24a (emphasis added). "That line of reasoning," FERC explains, "is similar to the Ninth Circuit's interpretation of *Mobile-Sierra* 'as the equivalent of an estoppel doctrine,' an interpretation that this Court rejected in *Morgan Stanley*." FERC Br. 13-14. For that reason too, the decision below cannot be reconciled with *Morgan Stanley*, and this Court should grant, vacate, and remand in light of that intervening decision.[5]

CONCLUSION

The petition for a writ of certiorari should be granted.

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[5] This Court remands in light of intervening cases even where litigants have raised those cases in seeking rehearing below. See, *e.g.*, *Keisler* v. *Hong Yen Gao*, 128 S. Ct. 345 (2007); *Johnson* v. *Potter*, 127 S. Ct. 3003 (2007); *Klinger* v. *Director, Dep't of Revenue*, 545 U.S. 1111 (2005). That reflects the reality that lower courts sometimes rely on this Court's GVR practice, rather than losing litigants' rehearing requests, to identify decisions that warrant reconsideration in light of this Court's intervening decisions.

Respectfully submitted.

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APPENDIX

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FERC Decisions Rejecting Filings With *Mobile-Sierra* Clauses

1. *Duke Energy Carolinas, LLC*, 123 FERC ¶61,201 at P10 & n.10 (May 23, 2008) (rejecting, in light of *Maine Pub. Utils. Comm'n* v. *FERC*, 520 F.3d 464 (D.C. Cir. 2008) (Pet. App. 1a-27a), provision of uncontested bilateral power purchase agreement that required future modification requests to meet *Mobile-Sierra*'s public-interest standard; stating that "the Commission would find acceptable a substitute provision that imposes on non-contracting third parties 'the most stringent standard permissible under applicable law'").

2. *Appalachian Power Co.*, FERC Docket No. ER08-763-000 (May 29, 2008) (similar order on review of uncontested bilateral full-requirements electric service agreement); *Appalachian Power Co.*, FERC Docket No. ER08-763-001 (Jan. 5, 2009) (accepting compliance filing following revision of agreement to replace *Mobile-Sierra* standard with clause requiring review of third-party challenges under the "most stringent standard permissible").

3. *Florida Power Corp.*, FERC Docket No. ER08-728-000 (May 29, 2008) (similar order on review of uncontested bilateral power sales agreement); *Florida Power Corp.*, FERC Docket No. ER08-728-001 (Sept. 10, 2008) (accepting compliance filing following revision of agreement to replace *Mobile-Sierra* standard with clause requiring review of third-party challenges under the "most stringent standard permissible").

4. *Westar Energy, Inc.*, 123 FERC ¶61,252 at P21 (June 6, 2008) ("*Westar I*") (similar order on review of bilateral cost-based formula-rate agreement where agreement was challenged by a third-party wholesale competitor and third-party retail customer; setting matter for hearing); *Westar Energy, Inc.*, 125 FERC ¶61,301

(Dec. 18, 2008) (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible").

5. *Florida Power Corp.*, FERC Docket Nos. ER08-671-000 *et al.* (similar order on review of uncontested bilateral service agreement); *Florida Power Corp.*, FERC Docket No. ER08-671-002 (Mar. 9, 2009) (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible").

6. *Southern Star Cent. Gas Pipeline, Inc.*, 124 FERC ¶61,016 at P14 (July 3, 2008) (similar order on review of uncontested multilateral settlement to adjust fuel and loss reimbursement percentages in shipping rates); *Southern Star Cent. Gas Pipeline, Inc.*, FERC Docket No. RP08-84-002 (Aug. 22, 2008) (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible").

7. *Westar Energy, Inc.*, 124 FERC ¶61,027 at PP21-22 (July 11, 2008) ("*Westar II*") (similar order on review of agreed-upon bilateral cost-based formula-rate agreement challenged by third-party wholesale competitor and third-party retail customer; setting matter for hearing); *Westar Energy, Inc.*, 125 FERC ¶61,301 (Dec. 18, 2008) (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible").

8. *Westar Energy, Inc.*, 124 FERC ¶61,057 at PP25-26 (July 17, 2008) ("*Westar III*") (similar order on review of four agreed-upon bilateral cost-based formula rate agreements challenged by third-party wholesale competitor and third-party retail customer; setting matter for hearing); *Westar Energy, Inc.*, 125 FERC ¶61,301 (Dec.

18, 2008) (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible").

9. *Midwest Indep. Sys. Operator, Inc.*, 124 FERC ¶61,074 at PP9-11 (July 21, 2008) (similar order on review of uncontested multilateral settlement of market-wide balancing authority agreement); *Midwest Indep. Sys. Operator, Inc.*, FERC Docket No. ER07-1372-012 (Dec. 4, 2009) (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible").

10. *Wisconsin Elec. Power Co.*, 124 FERC ¶61,076 at P4 (July 21, 2008) (similar order on review of uncontested multilateral agreement on distribution of decommissioning funds from sale of nuclear power plant); *Wisconsin Elec. Power Co.*, FERC Docket No. ER07-1192-001 (Aug. 21, 2008) (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible").

11. *Iroquois Gas Transmission Sys., L.P.*, 124 FERC ¶61,080 at P13 (July 23, 2008) (similar order on review of uncontested multilateral settlement of shipping tariff filing); *Iroquois Gas Transmission Sys., L.P.*, FERC Docket No. RP07-443-003 (Oct. 2, 2008) (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible").

12. *Allegheny Generating Co.*, 124 FERC ¶61,081 at P4 (July 23, 2008) (similar order on uncontested bilateral settlement of pumped-storage generation allocation agreement); *Allegheny Generating Co.*, FERC Docket No. ER07-1402-002 (Oct. 8, 2008) (accepting compliance filing following substitution of clause requiring review of

third-party challenges under the "most stringent standard permissible").

13. *NSTAR Elec. & Gas Corp.* v. *ISO New England, Inc.*, 124 FERC ¶61,083 at P5 (July 24, 2008) (similar order on review of uncontested tri-party settlement resolving complaint against ISO New England's administration of reliability-must-run agreement); *NSTAR Elec. & Gas Corp.* v. *ISO New England, Inc.*, FERC Docket No. EL07-68-001 (Jan. 5, 2009) (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible").

14. *Arizona Pub. Serv. Co.*, 124 FERC ¶61,088 at P4 (July 25, 2008) (similar order on review of uncontested multilateral settlement of revisions to open-access transmission tariff); *Arizona Pub. Serv. Co.*, FERC Docket No. ER07-1142-002 (Oct. 2, 2008) (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible").

15. *Westar Energy, Inc.*, 124 FERC ¶61,090 at PP23-25 (July 25, 2008) ("*Westar IV*") (similar order on review of 13 agreed-upon bilateral cost-based formula-rate agreements challenged by a third-party wholesale competitor, third-party retail customer, and third-party wholesale customer; setting matter for hearing); *Westar Energy, Inc.*, 125 FERC ¶61,301 (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible").

16. *Consumers Power Co.*, 124 FERC ¶61,093 at P4 (July 28, 2008) (similar order on review of uncontested multilateral settlement of title-transfer-tracking rate filing); *Consumers Power Co.*, FERC Docket No. PR97-1-006 (Oct. 29, 2008) (accepting compliance filing following

substitution of clause requiring review of third-party challenges under the "most stringent standard permissible").

17. *Entergy Servs., Inc.*, 124 FERC ¶61,100 at PP2-3 (July 29, 2008) (similar order on review of uncontested multilateral settlement of rate redetermination).

18. *PJM Interconnection, LLC*, 124 FERC ¶61,112 at PP20-21 (July 29, 2008) (similar order on review of contested multilateral partial settlement of cost responsibility for approved projects); *PJM Interconnection, LLC*, FERC Docket Nos. ER06-456-015 *et al.* (Oct. 15, 2008) (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible").

19. *Westar Energy, Inc.*, 124 FERC ¶61,171 at PP20-22 (Aug. 20, 2008) ("*Westar V*") (similar order on review of agreed-upon bilateral cost-based formula-rate agreements challenged by third-party wholesale competitor, third-party retail customer, and third-party wholesale customer); *Westar Energy, Inc.*, 125 FERC ¶61,301 (Dec. 18, 2008) (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible").

20. *Vermont Elec. Power Co.*, 124 FERC ¶61,178 at P3 (Aug. 22, 2008) (similar order on review of uncontested multilateral settlement of cost responsibility for transmission upgrade); *Vermont Elec. Power Co.*, FERC Docket Nos. ER07-459-003 *et al.* (Feb. 6, 2009) (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible").

21. *Wisconsin Power & Light Co.*, 124 FERC ¶61,179 at PP3, 5 (Aug. 22, 2008) (similar order on review of uncontested multilateral settlement of utility's proposed changes to its wholesale electric tariffs); *Wisconsin*

Power & Light Co., FERC Docket Nos. ER06-1517-002 *et al.* (Nov. 21, 2008) (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible").

22. *Enron Power Mktg., Inc., et al.*, 124 FERC ¶61,206 at P24 (Aug. 29, 2008) (similar order on review of uncontested multilateral settlement of proceedings to revoke Enron companies' authority to sell natural gas and energy at market-based rates); *Enron Parties & City of Seattle*, FERC Docket Nos. EL03-77-008 *et al.* (Oct. 3, 2008) (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible")

23. *Pub. Serv. Co. of N.M.* v. *Southwestern Pub. Serv. Co.*, 124 FERC ¶61,232 at P32 (Sept. 8, 2008) (similar order on review of uncontested bilateral partial settlement arising from interruptible-power service agreement and non-fuel-cost-adjustment clause in tariff rate challenged by third-party competitor).

24. *Pacific Gas & Elec. Co.*, 124 FERC ¶61,234 at PP4-5 (Sept. 10, 2008) (similar order on review of uncontested bilateral settlement of wholesale distribution and interconnection dispute).

25. *California Power Exch. Corp.*, 124 FERC ¶61,294 at P4 (Sept. 29, 2008) (similar order on review of uncontested multilateral settlement); *California Power Exch. Corp.*, EL03-223-004 (Nov. 26, 2008) (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible").

26. *Southern Cal. Edison Co.*, 125 FERC ¶61,012 at P5 (Oct. 3, 2008) (similar order on review of uncontested bilateral settlement of amounts owed under long-term agreement); *Southern Cal. Edison Co.*, 126 FERC

¶61,048 (Jan. 15, 2009) (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible").

27. *Westar Energy, Inc.*, 125 FERC ¶61,027 at PP23-24 (Oct. 10, 2008) ("*Westar VI*") (similar order on review of agreed-upon bilateral cost-based formula-rate agreements challenged by a third-party wholesale competitor, third-party retail customer, and third-party wholesale customer; setting matter for hearing).

28. *Duke Energy Carolinas, LLC*, FERC Docket No. ER08-1524-000 (Nov. 6, 2008) (rejecting uncontested bilateral partial requirements service agreement to the extent it provided for third-party challenges to be reviewed under *Mobile-Sierra*; requiring a compliance filing adopting the "most stringent standard permissible under the law" formulation).

29. *NorthWestern Corp.*, 125 FERC ¶61,179 at P24 (Nov. 14, 2008) (similar order on uncontested bilateral reserve services agreement).

30. *Aquila Merchant Servs., Inc., et al.*, 125 FERC ¶61,175 at P22 (Nov. 14, 2008) (rejecting, as incompatible with *Maine Public Utilities Commission*, provisions establishing *Mobile-Sierra* standard for future challenges to three contested multilateral settlement agreements resolving FERC's investigations of alleged market manipulation by three entities during the California energy crisis; suggesting "most stringent standard permissible under applicable law" as an "acceptable substitute provision"); *Powerex Corp.*, Docket Nos. EL03-166-005, *et al.* (Jan. 6, 2009) (accepting revisions); *Aquila Merchant Servs., Inc.*, FERC Docket Nos. EL03-138, *et al.* (Feb. 18, 2009) (same).

31. *Coral Power, LLC, et al.*, 125 FERC ¶61,176 at P19 (Nov. 14, 2008) (similar order on review of five con-

tested multilateral settlement agreements resolving FERC's investigations of alleged market manipulation by five companies during the California energy crisis); *Sempra Energy Trading LLC*, FERC Docket Nos. EL03-173-005, *et al.* (Feb. 18, 2009) (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible"); *Northern Cal. Power Agency*, FERC Docket No. EL03-196-006 (Feb. 18, 2009) (same); *Pub. Serv. Co. of N.M.*, FERC Docket No. EL03-200-007 (Feb. 18, 2009) (same); *City of Glendale, Cal.*, FERC Docket Nos. EL03-147-006, *et al.* (Feb. 18, 2009) (same).

32. *Modesto Irrigation Dist., et al.*, 125 FERC ¶61,173 (Nov. 14, 2008) (rejecting *Mobile-Sierra* standard for modification of two contested multilateral settlement agreements resolving FERC's investigations of alleged market manipulation during the California energy crisis; suggesting provision imposing the "most stringent standard permissible under applicable law" as an "acceptable substitute provision"); *Modesto Irrigation Dist.*, FERC Docket No. EL03-193-006 (Feb. 18, 2009) (accepting compliance filing following substitution of clause requiring review of third-party challenges under the "most stringent standard permissible").

33. *Modesto Irrigation Dist.*, 125 FERC ¶61,174 at P15 (Nov. 14, 2008) (similar order also with respect to contested multilateral settlement agreements resolving FERC's investigations of alleged market manipulation during the California energy crisis).

34. *Carolina Power & Light Co.*, FERC Docket No. ER09-9-000 (Nov. 24, 2008) (miscaptioned *Duke Energy Carolinas, LLC*) (rejecting *Mobile-Sierra* standard for modification of uncontested bilateral partial-requirements service agreement; requiring compliance filing providing for review of third-party challenges under "most stringent standard permissible"); *Carolina Power*

& Light Co., FERC Docket No. ER09-9-001 (accepting compliance filing).

35. *Florida Power Corp.*, FERC Docket No. ER09-250-000 (Dec. 10, 2008) (rejecting *Mobile-Sierra* standard for modification of uncontested bilateral full-requirements cost-based power sale agreement; requiring compliance filing providing for review of third-party challenges under "most stringent standard permissible").

36. *Carolina Power & Light Co.*, FERC Docket No. ER09-179-000 (Dec. 18, 2008) (rejecting *Mobile-Sierra* standard for modification of uncontested bilateral cost-based power sale agreement; requiring compliance filing providing for review of third-party challenges under "most stringent standard permissible"); *Carolina Power & Light Co.*, FERC Docket No. ER09-179-001 (accepting compliance filing).

37. *Norwalk Power, LLC*, 125 FERC ¶61,390 at P3 (Dec. 30, 2008) (approving uncontested settlement of reliability-must-run agreement where settlement adopted "most stringent standard permissible" formulation for third-party challenges, but requiring modification of settlement agreement to provide that, where parties agreed to ordinary just-and-reasonable review of changes proposed by one another, FERC would also be "bound to the 'just and reasonable' standard").

38. *Florida Power Corp.*, FERC Docket No. ER09-301-000 (Jan. 5, 2009) (rejecting *Mobile-Sierra* standard for modification of uncontested bilateral power sales agreement; requiring compliance filing providing for review of third-party challenges under "most stringent standard permissible").

39. *Devon Power LLC*, 126 FERC ¶61,027 at P5 (Jan. 15, 2009) (on remand from decision below) (conditioning approval of multilateral settlement agreement on submission of a compliance filing "revising the standard of

review applicable to non-settling third parties, consistent with the court's decision").

40. *PacifiCorp*, FERC Docket No. ER09-380-000 (Feb. 3, 2009) (rejecting *Mobile-Sierra* standard for modification of uncontested bilateral large generator interconnection agreement; requiring compliance filing providing for review of third-party challenges under "most stringent standard permissible").

41. *PacifiCorp*, FERC Docket No. ER09-511-000 (Mar. 2, 2009) (rejecting *Mobile-Sierra* standard for modification of uncontested bilateral facilities-maintenance agreement; requiring compliance filing providing for review of third-party challenges under "most stringent standard permissible").

AMICUS CURIAE BRIEF

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IN THE
SUPREME COURT OF THE UNITED STATES

NRG POWER MARKETING, LLC, *ET AL.*,
Petitioners,

v.

MAINE PUBLIC UTILITIES COMMISSION, *ET AL.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

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BRIEF OF AMICI CURIAE AMERICAN PUBLIC POWER ASSOCIATION AND NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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BRIEF OF *AMICI CURIAE* AMERICAN PUBLIC POWER ASSOCIATION AND NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION OPPOSING PETITION FOR A WRIT OF CERTIORARI

INTEREST OF AMICI[1]

The American Public Power Association (APPA) represents the nation's more than 2,000 not-for-profit, publicly-owned electric utilities, which do business in every state except Hawaii. Public power systems own about 10 percent of the nation's electric generating capacity, and provide over 15 percent of all kilowatt-hours of electricity sold to ultimate customers. Sixty-six New England public power systems are APPA members.

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[1] Counsel of record for all parties received notice at least 10 days prior to the due date of the *amici curiae*'s intention to file this brief, and the parties consented to the filing of this brief. No counsel for a party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than *amici curiae*, its members, or its counsel made a monetary contribution to its preparation or submission.

The National Rural Electric Cooperative Association (NRECA) represents the nation's 930 not-for-profit, customer-owned rural electric cooperatives serving more than 40 million end users in 47 states. Of those 930 cooperatives, 64 are generation and transmission cooperatives that are owned by and sell power to their member distribution cooperatives. NRECA has 7 members in New England.

Both associations' members participate in wholesale power markets as buyers *and* sellers. The associations assert that Court review of the decision below[2] is not warranted.

SUMMARY OF ARGUMENT

The *Mobile-Sierra* doctrine[3] holds that freely negotiated contracts between sophisticated parties with presumptively equal bargaining power are presumed just and reasonable "as between the two [contracting parties]." *Morgan Stanley Capital Group Inc. v. Pub. Util. Dist. No. 1 of Snohomish County* (*Snohomish*), 554 U.S. ___, 128 S. Ct. 2733,

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[2] *Me. Pub. Utils. Comm'n v. FERC* (*Maine Public*), 520 F.3d 464 (D.C. Cir. 2008) (Pet. App. A), *reh'g denied*, No. 06-1403 (D.C. Cir. Oct. 6, 2008).

[3] *See United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.* (*Mobile*), 350 U.S. 332 (1956); *FPC v. Sierra Pac. Power Co.* (*Sierra*), 350 U.S. 348 (1956).

2746 (2008) (internal quotation omitted). That presumption arises once the contracting parties reach agreement; it does not depend on FERC's review and approval. *Id.* at 2745.

This case is about whether the *Mobile-Sierra* presumption—the linchpin of which is a freely negotiated agreement—can be imposed by contracting parties upon *non*-contracting parties. The D.C. Circuit concluded correctly that neither the parties to a contested settlement agreement nor the Federal Energy Regulatory Commission (FERC) may elevate the showing that non-settling parties must make to demonstrate that a rate has become unreasonable as to them.

In the proceeding below, ISO New England (ISO-NE) filed a tariff establishing market-wide rates, which FERC suspended and set for hearing. ISO-NE and a subset of intervenors reached a settlement purporting to set rates for all market participants, whether or not they agreed to the settlement. Some litigants objected.

Petitioners acknowledge that the contested settlement created no initial presumption of reasonableness as to non-parties. They concede, as they must, that FERC correctly reviewed the settlement under the ordinary just and reasonable standard. *E.g.*, *Mobil Oil Corp. v. FPC* (*Mobil*), 417 U.S. 283, 312 (1974); *Laclede Gas Co. v. FERC* (*Laclede*), 997 F.2d 936, 944 (D.C. Cir. 1993).

While conceding that no presumption applied during FERC's initial review of the contested settlement, Petitioners nonetheless contend that FERC could approve a settlement provision creating a forward-looking *Mobile-Sierra* presumption applicable to later challenges, whether brought by settling or non-settling parties. *Snohomish* teaches, however, that the *Mobile-Sierra* presumption arises from parties' consent, not FERC's approval, and that, where *Mobile-Sierra* applies, the timing of a challenge is irrelevant. The same absence of consent that precluded the application of a presumption during FERC's review of the contested settlement also bars its application to subsequent non-party challenges.

Mobile-Sierra's inapplicability in this case makes sense considering the doctrine's role as a "reasonable accommodation between the conflicting interests of contract stability on the one hand and public regulation on the other." *Mobile*, 350 U.S. at 344. As applied to non-settling parties, the rates at issue here are not contract rates. They are tariff rates imposed pursuant to a settlement that the non-settling parties did not sign. *Mobile-Sierra* has never extended to unilaterally imposed rates, and the effort to employ *Mobile-Sierra* offensively here—first imposing rates on non-settling parties and then erecting a presumption of reasonableness making those rates harder to challenge later—is unsupportable.

Petitioners and supporting *amici*[4] advance exaggerated claims that the decision below "undoes" *Snohomish* by allowing third-party surrogates to challenge unsatisfactory agreements, and will "destabilize the Nation's power markets," EPSA Br. 1. In fact, the decision below has not even "destabilize[d]" the settlement in *this case* or the resulting capacity market, which ISO-NE has touted as a success. Moreover, FERC and appellate courts will be able to distinguish legitimate third-party claims from pretextual or unsupported ones. Indeed, the panel below included two judges who had already encountered—and dismissed—such claims.

Petitioners and supporting *amici* ignore that, even under an ordinary just-and-reasonable standard, FERC does not take contract modification lightly. In considering whether changed circumstances have caused a rate to become unjust and unreasonable, FERC must balance consumer and investor interests, and may not simply disregard investments reasonably made in reliance on expected rate continuity. Consequently, billions have been invested in transmission or generation facilities priced under tariffs or contracts that are subject to an ordinary just-and-reasonable standard.

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[4] *See* Br. of the Elec. Power Supply Ass'n as *Amici Curiae* in Support of Pet. Cert., Dec. 22, 2008 (EPSA Br.).

Exaggerated claims about the need for "certainty" do not justify expanding *Mobile-Sierra* to insulate rates imposed on *non*-consenting parties.

ARGUMENT

I. *MAINE PUBLIC* ACCORDS WITH PRECEDENT.

Petitioners wrongly claim that the decision below rests on a legal theory rejected by *Snohomish* and will upset decades of settled precedent. Pet. for Writ of Cert. of NRG Power Mktg., LLC, at 23, Nov. 21, 2008 (Pet.).

A. Maine Public does not conflict with *Snohomish*'s holding that there is one statutory standard.

Petitioners argue that *Maine Public* wrongly treated the public-interest standard as an "atextual exception to the statutory just and reasonable standard," when *Snohomish* clarified that it is merely a "differing *application* of that ... standard to contract rates," Pet. 12 (internal quotations omitted). In doing so, they elevate semantics over substance. While *Maine Public* used pre-*Snohomish* nomenclature, *see* 128 S. Ct. at 2740, its holding does not depend on treating the public-interest standard as a statutory exception. Restating its holding using *Snohomish*'s terminology, *Maine*

Public held that contracting parties may not erect a presumption of reasonableness as against non-contracting parties, thereby making it harder for them to challenge the parties' contract, either initially or in light of changed circumstances.

B. Contested settlements are not presumed reasonable, because the factual basis for that presumption is missing.

Petitioners contend that contracting parties may compel FERC to presume the reasonableness of rates set forth in a contested settlement as against parties who opposed the settlement and refused to accept the risk allocation embodied in it.[5] APPA and NRECA are aware of no judicial precedent for that position.

In 1974, this Court established the "correct legal principles" governing the Commission's assessment of "settlement proposal[s] that lack[] unanimous agreement ...." *Mobil*, 417 U.S. at 312.

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[5] *Compare* Pet. 17 n.6, discussing Judge Posner's characterization of fixed-price contracts as "explicit" (and, we might add, voluntary) assignments of market risk as between buyers and sellers, who "[have] only [themselves] to blame" if the contracts become unprofitable. That characterization does not apply to non-contracting parties.

That some parties agreed to the deal "did not, of course, establish without more the justness and reasonableness of its terms." *Id.* at 312-13. Instead, the Court explained:

> "If a proposal enjoys unanimous support from all of the immediate parties, it could certainly be adopted as a settlement agreement if approved in the general interest of the public. But even if there is a lack of unanimity, it may be adopted as a resolution *on the merits*, if FPC makes an independent finding supported by 'substantial evidence on the record as a whole' that the proposal will establish 'just and reasonable' rates ...."

Id. at 314 (quoting *Placid Oil Co. v. FPC*, 483 F.2d 880, 893 (5th Cir. 1973), *aff'd sub nom. Mobil*, 417 U.S. 283, underlined emphasis added). Thus, the Court affirmed the Fifth Circuit's inquiry into "whether, viewing the terms of the proposal not as a traditional settlement but as a result of an administrative decision, it falls within that 'zone of reasonableness' which is supported by 'substantial evidence on the record as a whole.'" *Placid Oil*, 483 F.2d at 894.

Numerous D.C. Circuit cases are in accord. *E.g.*, *Kelley ex rel. Mich. Dep't of Natural Res. v. FERC*, 96 F.3d 1482, 1489 (D.C. Cir. 1996) ("[A]

settlement that is forced onto a party is effectively converted into a decision 'on the merits.'"); *Laclede*, 997 F.2d at 946 ("reject[ing] the notion that any settlement, solely because of its status as such, is reasonable"); *Tejas Power Corp. v. FERC*, 908 F.2d 998, 1003-04 (D.C. Cir. 1990); *Consol. Gas Supply Corp. v. FERC*, 606 F.2d 323, 330 (D.C. Cir. 1979) ("The standard for judicial review of [a FERC order on] a contested settlement proposal is ... whether the Commission has made an independent rate determination supported by substantial evidence ...").[6]

Contested settlements create no presumption of reasonableness because the element essential to that presumption—consent—is missing. FERC must therefore make an "independent finding ... that the proposal will establish 'just and reasonable' rates," *Mobil*, 417 U.S. at 314 (internal quotation omitted).

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[6] In making that independent determination, FERC may accord "some weight" to the number of customers supporting or not opposing the agreement, but a headcount is not dispositive. 997 F.2d at 946.

C. FERC approval does not create a *Mobile-Sierra* presumption.

While Petitioners concede that FERC correctly reviewed the contested settlement under the "ordinary just-and-reasonable standard," Pet. 13 n.4 and 7-8, they contend that settling parties may create forward-looking presumptions, applicable to later third-party challenges, by obtaining FERC approval of a *Mobile-Sierra* provision. *Id.*[7]

Snohomish itself foreclosed such claims by rejecting arguments that the standard for evaluating contract-modification requests depends on whether FERC previously reviewed the contract. 128 S. Ct. at 2745. To paraphrase Petitioners, if a *Mobile-Sierra* presumption applies, it arises "once the contract is signed 'regardless of when [it] is reviewed.'" Pet. 5 (quoting 128 S. Ct. at 2737). The converse is also true. If no presumption applies when FERC initially considers a contested settlement, none can be established by FERC's approval

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[7] Petitioners label section 4C of the settlement a "*Memphis* clause." Pet. 7. That description is apt only insofar as section 4C preserved the *settling parties'* ability to seek modifications under the ordinary just-and-reasonable standard. As to *non*-settling parties (who nonetheless pay the market-wide rates established by the settlement), section 4C attempted to create a presumption where none existed, and the "*Memphis* clause" label is inapt.

of it. To hold otherwise would be to treat *Mobile-Sierra*, contrary to *Snohomish*'s teaching, 128 S. Ct. at 2746, as an estoppel doctrine precluding FERC from modifying an agreement it once approved.[8]

D. *Maine Public* respects the *Mobile-Sierra* doctrine's contractual foundations.

Maine Public is consistent with *Mobile-Sierra*'s contractual foundations, while Petitioners' view conflicts with those premises. As explained in *Snohomish*, the Federal Power Act (FPA), 16 U.S.C. §§ 791a-825r, "'departed from the scheme of purely tariff-based regulation and acknowledged that contracts between commercial buyers and sellers could be used in ratesetting.'" 128 S. Ct. at 2738 (quoting *Verizon Commc'ns, Inc. v. FCC* (*Verizon*), 535 U.S. 467, 479 (2002)). It did so because, "'[i]n wholesale markets, the party charging the rate and the party charged [are] often sophisticated businesses enjoying presumptively equal bargaining power, who could be expected to negoti-

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[8] Contrary to Petitioners' suggestion (Pet. 25), *Snohomish*'s rejection of the estoppel analogy severed neither *Mobile-Sierra*'s contractual underpinnings nor the fundamental requirement of consent. The rejected analogy focused on whether FERC's initial rate approval estops later evaluation of whether the rate remains just and reasonable despite changed circumstances, 128 S. Ct. at 2746, exactly the sort of estoppel urged by Petitioners here.

ate a "just and reasonable" rate *as between the two of them.*'" *Id.* at 2746 (emphasis added, quoting *Verizon*, 535 U.S. at 479). The FPA thus permits utilities to set rates "with individual electricity purchasers through bilateral contracts," *id.* at 2738, and *Mobile-Sierra* requires FERC to presume that "the rate[s] set out in [such] freely negotiated wholesale-energy contract[s] meet[] the 'just and reasonable' requirement ...." *Id.* at 2737.

But while sophisticated buyers and sellers can look out for their own interests and trade other benefits in exchange for rights to mount later challenges—giving rise to a presumption that the resulting agreement is reasonable "'as between the two of them,'" 128 S. Ct. at 2746—their agreement establishes no presumption as to *other* entities. *See Verizon*, 535 U.S. at 479 ("[T]he principal regulatory responsibility [is] not to relieve *a contracting party* of an unreasonable rate....") (emphasis added).

Here, remarkably, Petitioners seek to hold sophisticated entities to bargains they chose *not* to make—and then to enshrine the "deal" with *Mobile-Sierra* presumptions. As Commissioners Kelly and Wellinghoff noted, Pet. App. D. 228a, the proceedings here began with a unilateral tariff filing to establish a region-wide capacity market. After some litigants settled, the resulting market rules were incorporated into ISO-NE's tariff, which binds

all wholesale market participants, including non-settling parties. From a non-party's perspective, the imposition of capacity market rules and rates to which they did not agree is a form of tariff-based regulation, which has never been subject to contract-based *Mobile-Sierra* presumptions. The court below correctly rejected the attempt to prevent non-settling parties from seeking review, under an ordinary just-and-reasonable standard, of rates that they are required to pay but to which they did not agree.[9]

E. Maine Public is consistent with Petitioners' cited cases.

Contrary to Petitioners' assertions, Pet. 16, the D.C. Circuit's decision does not upset decades of settled precedent. First, none of Petitioners' cited cases involved a situation like this one, where par-

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[9] The error in Petitioners' attempt to establish presumptions against non-party contract-modification requests is further illustrated by *Snohomish*'s discussion of the role of *Memphis* clauses. As the Court explained, 128 S. Ct. at 2739, parties may "contract out of the *Mobile-Sierra* presumption ..." by specifying in their agreements the circumstances under which each would be permitted to seek a rate change unilaterally. *Id.* Under Petitioners' view of the law, while parties may "contract out" of the *Mobile-Sierra* presumption, *id.*, those who have never contracted *into* it remain subject to it nonetheless.

ties to a contested settlement seek to set market-wide rates, applicable to both settling and non-settling parties, and to harden those rates against future non-party challenges.

Second, while FERC's decisions have been inconsistent, FERC often has rejected invocations of *Mobile-Sierra* as an impediment to non-party contract modification requests.[10] In *PJM Interconnection, LLC* (*PJM*), 96 F.E.R.C. ¶ 61,206, at 61,878 & n.13 (2001), FERC explained that:

> *Mobile-Sierra* does not speak to situations ... where a non-party ... seeks changes under section 206 [16 U.S.C. § 824e].[13] Under PPL's interpretation, parties to a contract who agree among themselves not to seek rate changes would be able to bind not only one another, but also other entities who are not parties to that contract (and did not receive the contractual benefits in exchange for which the parties traded away their

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[10] According to Petitioners, the court of appeals "did not dispute that FERC had long applied *Mobile-Sierra* to third-party challenges." Pet. 12. In fact, the court expressly noted that FERC has accepted *Mobile-Sierra* provisions applying the public interest standard to non-contracting parties, "only since 2002." Pet. App. A. 23a.

right to seek rate changes). This result is not what the Supreme Court intended in *Mobile-Sierra*.

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[13] See, e.g., Southern Company Services, Inc., 67 F.E.R.C. ¶61,080, at pp. 61,227-28 (1994); accord, Cities of Anaheim and Riverside v. Deseret Generation & Transmission Co-operative, 90 F.E.R.C. ¶61,236, at p. 61,755 (2000); Carolina Power & Light Co., 67 F.E.R.C. ¶61,074, at p. 61,205 (1994); see also Northeast Utilities Service Co., 66 F.E.R.C. ¶61,332, at pp. 62,081-88, reh'g denied, 68 F.E.R.C. ¶61,041 (1994), aff'd, 55 F.3d 686, 689-93 (1st Cir. 1995) ....

Indeed, for at least a decade prior to 2002-03, FERC refused to accept settlement provisions subjecting non-parties—or FERC acting *sua sponte* on their behalf—to a *Mobile-Sierra* presumption.[11]

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[11] In addition to the cases cited in footnote 13 of *PJM*, *see ITC Holdings Corp.*, 102 F.E.R.C. ¶ 61,182, P 77 (distinguishing market-based rate agreements, like those at issue in *Snohomish*, from contracts that "set not only the respective rights and obligations of the contractual parties, but also the rates that third parties will pay"), *reh'g denied*, 104 F.E.R.C.

FERC considered such provisions to be "contrary to Commission precedent and to the Commission's statutory mandate." *Carolina Power & Light Co.*, 67 F.E.R.C. at 61,205.

Even after 2002-03, FERC sometimes rejected settlement provisions purporting to require non-parties or FERC to satisfy the public-interest version of the just-and-reasonable standard when seeking contract modifications. For example, while Reliability Must-Run (RMR) agreements superficially resemble bilateral purchase-sale agreements, they are negotiated for system reliability reasons by not-for-profit ISOs, which lack cost-reduction incentives because they pass on all of their costs to consumers. *NSTAR Elec. & Gas Corp. v. FERC*, 481 F.3d 794, 803 (D.C. Cir. 2007). FERC has determined that RMR agreements harm markets and should be accepted only as a "last resort." *See*

¶ 61,033 (2003); *Westar Generating, Inc.*, 100 F.E.R.C. ¶ 61,255, P 6 (2002); *Niagara Mohawk Power Corp.*, 97 F.E.R.C. ¶ 61,018, at 61,060 (2001); *GPU Energy*, 94 F.E.R.C. ¶ 61,336, at 62,241 (2001); *Turlock Irrigation Dist.*, 88 F.E.R.C. ¶ 61,322, at 61,978 (1999); *Mont. Power Co.*, 88 F.E.R.C. ¶ 61,019, at 61,051 (1999); *New England Power Co.*, 81 F.E.R.C. ¶ 61,281, at 62,371 (1997), *rch'g denied*, 83 F.E.R.C. ¶ 61,265 (1998), *aff'd sub nom. Town of Norwood v. FERC*, 202 F.3d 392 (1st Cir. 2000); *Sierra Pac. Power Co.*, 77 F.E.R.C. ¶ 61,048, at 61,186-87 (1996); *Wis. Pub. Serv. Corp.*, 69 F.E.R.C. ¶ 61,209, at 61,829 (1994); *Ne. Utils. Serv. Co.*, 67 F.E.R.C. ¶ 61,335 (1994).

Bridgeport Energy, LLC, 118 F.E.R.C. ¶ 61,243, P 41 (2007). While FERC has accepted settlements allowing such agreements to go into effect, it has rejected settlement provisions subjecting future challenges to those agreements to the public-interest application of the just-and-reasonable standard. *Id.* (holding that it "would be inconsistent with our duty under the [FPA]" to accept such provisions); *see also PSEG Power Co.*, 119 F.E.R.C. ¶ 61,168 (2007); *Milford Power Co.*, 119 F.E.R.C. ¶ 61,167, *reh'g denied*, 121 F.E.R.C. ¶ 61,042 (2007).

FERC also has refused to accept *Mobile-Sierra* provisions seeking to insulate aspects of the relationship between ISOs and transmission-owning public utilities (TOs). For example, in 2003, a group of New England TOs and ISO-NE entered into an agreement to facilitate formation of a regional transmission organization (RTO). FERC rejected the TOs' proposal that "the *Mobile-Sierra* 'public interest' standard govern FERC review of termination and withdrawal" from the RTO, *Maine Public Utilities Commission v. FERC*, 454 F.3d 278, 281 (D.C. Cir. 2006), finding (*inter alia)* that such withdrawal could "have a substantial [deleterious] impact on other market participants and the markets themselves," *id.* at 286 (internal quotation omitted). The D.C. Circuit affirmed, noting that "there is no expectation of contract stability when," among other things, "that contract is a complex

agreement establishing a new regional structure impacting all market participants." *Id.* at 284.

These cases are consistent not only with *Snohomish*, for the reasons explained above, but also with the courts of appeals decisions cited by Petitioners. First, Petitioners cite *Northeast Utilities Service Co. v. FERC* (*Northeast Utils. I*), 993 F.2d 937 (1st Cir. 1993), and *Boston Edison Co. v. FERC*, 233 F.3d 60 (1st Cir. 2000), for the proposition that FERC, which is not a contracting party, must overcome the *Mobile-Sierra* presumption in every instance before modifying a contract. Pet. 26. In fact, those cases illustrate the distinction drawn here and in the FERC cases cited above: FERC must presume that contracts are reasonable as to those who sign them—and may modify them to protect contracting parties only if the failure to do so would harm the public. They do not stand for Petitioners' contention that FERC must presume reasonableness as to *non*-parties and may modify contracts for their protection only upon a heightened, public-interest showing.

In *Northeast Utils. I*, FERC conditioned its approval of a proposed merger on modification of certain rate schedules filed in connection with the merger, including removal of language subjecting FERC to a public-interest standard for future rate changes. 993 F.2d at 960. The First Circuit remanded. Agreeing that "[t]he most attractive case

for affording additional protection, despite the presence of a contract, is where the protection is intended to safeguard the interests of third parties," the court considered that protection to be limited to the "protection of outside parties from 'undu[e] discriminat[ion]' or imposition of an 'excessive burden.'" *Id.* at 961 (citation omitted). "If there is some reason for departing from this public interest standard as framed by the Supreme Court," the First Circuit held, "the Commission has not supplied it." *Id.*

On remand, FERC better explained its reasoning and required the same contract modifications. The First Circuit affirmed:

> FERC has responded to our concerns by explaining how the disputed contractual terms may harm third parties to the contract. It no longer relies so heavily upon the possibility that the contract may favor one party over another. For example, the Commission found the automatic rate-of-return-on-equity adjustment provision unacceptable because *third parties* may ultimately bear the burden of a rate component that does not reflect actual capital market conditions. Likewise, the "blank check" given owners of the power plant to determine the decommissioning costs

> for themselves under New Hampshire law is impermissible because it may be cashed at the expense of non-parties to the contract.

Ne. Utils. Serv. Co. v. FERC (*Northeast Utils. II*), 55 F.3d 686, 692 (1st Cir. 1995). The First Circuit required no showing that "unequivocal public necessity" demanded the contract modifications to avoid "serious harm to the public interest," Pet. 26. Instead, it affirmed FERC's modification of the contracts because the agency had explained "how the disputed contractual terms may harm third parties ...." 55 F.3d at 692.

Boston Edison involved FERC's *sua sponte* reduction of the return on equity (ROE) set forth in two bilateral contracts between a public utility seller and individual purchasers. 233 F.3d at 61, 63. Unlike the contested settlement in this case, the *Boston Edison* contracts did not establish rates paid by all wholesale-market customers, including non-consenting parties. In modifying the ROE, FERC did exactly what *Sierra* said FERC could not do: assume that a contract rate is unjust and unreasonable simply because it produces a return that is unfair to one of the contracting parties. FERC made no attempt to illustrate how non-contracting parties might be harmed, and the First Circuit remanded to FERC for further proceedings. On remand, the parties settled. *Boston Edison Co.*, 96

F.E.R.C. ¶ 61,290 (2001). *Boston Edison* thus says nothing about whether contracting parties may establish a presumption making it more difficult for *non*-parties to demonstrate that an agreement is unjust and unreasonable.

Petitioners' other cases are even less relevant. *Boroughs of Chambersburg v. FERC*, 580 F.2d 573 (D.C. Cir. 1978), *Public Service Co. of Indiana, Inc. v. FERC*, 575 F.2d 1204 (7th Cir. 1978), and *Town of Norwood v. FERC*, 587 F.2d 1306 (D.C. Cir. 1978), all involved attempts to resist public utility rate increases, permitted by applicable *Memphis* clauses, on grounds that the increase was unduly discriminatory compared to unchanged rates under other customers' contracts. *Mobile-Sierra*'s only relevance to those cases was to explain why the public utilities did not also increase the other customers' rates.

Finally, *Wisconsin Public Power Inc. v. FERC*, 493 F.3d 239 (D.C. Cir. 2007), resolved tensions between long-standing, bilateral transmission service agreements and proposed tariff provisions implementing new wholesale-market and transmission-congestion management mechanisms. Because the new procedures would disrupt the existing agreements, FERC required a carve-out for existing agreements that could not be modified unilaterally. *Id.* at 255. In other words, in *Wisconsin*, parties to long-standing bilateral contracts (to

which they had consented) invoked *Mobile-Sierra* defensively to protect their agreements from being overridden by tariff. Here, the settling parties would use *Mobile-Sierra* offensively to subject non-settling parties to rates they never agreed to pay and hold them to *Mobile-Sierra* restrictions on future rate challenges. *Maine Public*, decided by a panel that included one of the *Wisconsin* judges, correctly understood that *Mobile-Sierra* neither requires nor justifies such a result.

II. *MAINE PUBLIC* WILL NEITHER UNDERMINE NOR ALLOW EVASION OF *SNOHOMISH*.

Petitioners claim that *Maine Public* "threatens to turn [*Mobile-Sierra*] into a legal relic that applies only when rate challenges are brought by the direct counterparties in a contract." Pet. 16. That would be problematic, Petitioners argue, because "*Mobile-Sierra* cannot provide contractual certainty or stability" if its reasonableness presumption runs only to the contracting parties, while allowing "contract modification under a less rigorous standard in challenges brought by *anyone* else." *Id.* at 15. Petitioners raise the prospect of millions of "potential surrogates" seeking contract-rate changes under more lenient standards than would apply to challenges by contracting parties themselves. *Id.* at 19.

Petitioners offer no bases for these overblown claims. First, the use of surrogates to evade restrictions agreed to by contracting parties is unlikely. Although third-party protection always has afforded the "most attractive case" for contract modification, *Northeast Utils. I*, 993 F.2d at 961, FERC itself has observed that "[m]ost decisions involving *Mobile-Sierra* ... involve a request by one of the signatories to the contract at issue seeking to change the terms of the contract." *PJM*, 96 F.E.R.C. at 61,878 n.13.[12]

Second, Petitioners greatly overstate the prospects for contract modification under an ordinary just-and-reasonable standard. *E.g.*, Pet. 19 ("Subjecting fixed-price contracts to midstream abrogation if changing market conditions make one side of the contract (even temporarily) unattractive to any non-contracting entity destroys the purpose of those contracts."). FERC does not take contract abrogation lightly under *any* standard. *E.g.*, *Nev. Power Co. v. Duke Energy Trading & Mktg., LLC*, 100 F.E.R.C. ¶ 61,273, P 17 (2002) ("By emphasizing that a complainant bears a heavy burden of proof, we stated the obvious that the sanctity of

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[12] In any case, worries over challenges by contract-party surrogates would not justify derogation of FPA protections for genuinely independent non-parties—including, as in this case, protection of customers required to pay rates to which they did not agree.

contracts is presumed and that the Commission will not lightly undo the terms of existing contracts regardless of the applicable standard of review."); Pet. App. D 238a ("[A] challenger or the Commission acting *sua sponte* must prove that circumstances have changed so dramatically that the tariff provision has become unjust and unreasonable. This does not happen often."). Indeed, on remand from the decision below, FERC reiterated that "[n]on-parties to this settlement will have a high burden should they seek to modify the settlement in the future under a just and reasonable standard." *Devon Power LLC*, 126 F.E.R.C. ¶ 61,027, P 6 (2009).

While *amici* for Petitioners claim that "non-contracting third parties can be expected to challenge virtually any contract," EPSA Br. 15, they cite just four complaints, *id.* at 9-10, and fail to note that FERC dismissed or denied them all without evidentiary hearings. One was dismissed following settlement. *Ill. ex rel. Madigan v. Exelon Generation Co.*, 121 F.E.R.C. ¶ 61,015 (2007). Three, filed by a single party, were denied on grounds that the complainant "failed to present sufficient evidence to demonstrate that the contract[s] [are] unjust and unreasonable or should otherwise be abrogated"), *Californians for Renewable Energy, Inc. v. California Public Utilities Commission*, 120 F.E.R.C. ¶ 61,272, P 50 (2007) (Docket No. EL07-50) *and* 119 F.E.R.C. ¶ 61,058, P 45 (2007) (Docket

Nos. EL07-37 and EL07-40), *pet. for review filed sub nom. Californians for Renewable Energy v. FERC*, No. 08-70010 (9th Cir. filed Jan. 2, 2008), *dismissed in part* (9th Cir. Apr. 28, 2008).

Similarly, in *Potomac Electric Power Co. v. FERC* (*Potomac*), 210 F.3d 403 (D.C. Cir. 2000), the D.C. Circuit affirmed FERC's rejection of a party's contract-modification claims, including those dressed up as requests for *sua sponte* action to protect third parties:

> Emphasizing that it "does not take contract modification lightly," FERC reasoned that the mere fact that PEPCO was subject to higher rates under its agreement with APS than it would be under APS's OATT was insufficient reason for abrogating an agreement that PEPCO had fully supported at the time of filing.... FERC also rejected PEPCO's request that it act *sua sponte* to reduce the rates for the benefit of PEPCO's ratepayers, reasoning that it would be inappropriate to convert PEPCO's unilateral request for reformation into a FERC-initiated contract modification where the parties' agreement contained a *Mobile-Sierra* provision,

> and where PEPCO had failed to satisfy the public interest standard.

210 F.3d at 406. In other words, both FERC and an appellate panel including two of the *Maine Public* judges have made short work of unmeritorious complaints and attempted end-runs like those the Petitioners fear. The Court should not constrain FERC's ability to redress harm imposed on legitimately aggrieved non-parties in an effort to guard against unsupported or pretextual claims with which FERC already is well equipped to deal.

III. *MAINE PUBLIC* WILL NOT DETER INVESTMENT.

Petitioners and *amici* express concern that the decision below will deter needed investment in generation facilities. *E.g.*, EPSA Br. 5. Using this case as an example, Petitioners claim that "the auction pricing mechanism ... produces voluntary agreements to provide capacity three years in the future, ... [b]ut the promise to pay the auction amounts cannot provide the necessary incentive [to invest in new facilities] if the promise can be revisited continuously in light of changing circumstances." Pet. 20. Petitioners and *amici* argue that allowing non-party rate challenges under an ordinary just-and-reasonable standard will shatter the "contract certainty" necessary for investment, adding that the Court must not undermine investor confidence just when an economic crisis has nearly

frozen capital markets and massive infrastructure investment will be needed to support development and delivery of the output of new renewable-fuel generation resources. *E.g.*, Pet. 22-23.

As national organizations representing thousands of load-serving utilities of various sizes, including many who sign long-term contracts to support construction of new generation resources, APPA and NRECA have as much interest as Petitioners and their supporting *amici* in contract stability and a healthy investment environment. But APPA and NRECA do not subscribe to the overblown claims advanced by Petitioners and supporting *amici*.

First, as noted above, FERC does not take contract modification lightly even under the ordinary just-and-reasonable standard. Petitioners overlook that, in applying that standard, FERC must demonstrate to a reviewing court's satisfaction that it has balanced consumer and investor interests. Regardless of the applicable standard, FERC may not lightly disregard investments made in reliance on previously determined prices. Nor does FERC have a record of doing so. *See New York v. FERC*, 535 U.S. 1, 19 n.15 (2002).

Second, Petitioners offer no empirical support for their assumption that the ordinary just-and-reasonable standard deters investment, and the evidence is to the contrary. Here, although the

D.C. Circuit required FERC to modify a settlement that was conditioned on acceptance *without* modification, not a single settling party has sought to invalidate the settlement following the court's decision.[13] Instead, ISO-NE finalized and filed the applicable market rules (which FERC accepted), and has conducted two annual auctions in which both generation and demand-side resources actively participated and which ISO-NE has touted as a success.[14]

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[13] Section 2 conditioned the settlement agreement on FERC's approval of it without modification or condition. If FERC's approval was conditional, the agreement would terminate unless the parties ratified the change or negotiated acceptable amendments within 30 days. On October 6, 2008, the D.C. Circuit denied rehearing of its order requiring FERC to modify the settlement. On January 15, 2009, FERC issued an order directing the submission of a compliance filing revising the standard of review applicable to non-settling parties. The parties' February 17, 2009 compliance filing acknowledged that, "notwithstanding [the Settlement's] original provisions," and subject to the Court's action (if any) in this case, § 4C of the Settlement will not apply to non-parties. Report of Compliance of ISO NE and New England Power Pool, Attach. B, Compliance Statement, at 1, *Devon Power LLC*, Docket No. ER03-563-065 (Feb. 17, 2009), *available at* FERC eLibrary Accession No. 20090218-0153. Comments on the Compliance Statement were due March 10, 2009, but none were filed.

[14] Press Release, ISO-NE, New England's Second Power Resource Auction Produces Positive Outcomes for the Region (Dec. 10, 2008), *available at* http://www.iso-ne.com/nwsiss/

More generally, Petitioners ignore the many billions of dollars invested under tariff rates subject to change using an ordinary just-and-reasonable standard. Notably, most transmission service is provided under tariffs at cost-of-service rates that are subject to modification using an ordinary just-and-reasonable standard, and many billions have been invested (and continue to be invested) in transmission facilities whose costs are recovered through such rates. For example, in California, from 1998 through 2006, $8.2 billion was invested in more than 400 transmission projects.[15] In New England, between 2002 and 2006, transmission projects totaling $833 million were placed in service, *id.*, while more than $1 billion was invested in transmission in 2008 alone.[16]

Finally, Petitioners' claims that *Maine Public* has produced "disarray in the industry" (Pet. 22) are refuted by the very settlements that Petitioners cite in support of them. As Petitioners note, in the

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pr/2008/final_fca2_results_121008.pdf.

[15] ISO/RTO Council, *Progress of Organized Wholesale Electricity Markets in North America: A Summary of 2006 Market Data from 10 ISOs & RTOs*, at 5 (Oct. 16, 2007), *available at* http://tiny.cc/c16AR or through http://www.isorto.org, (under "Documents and Issues").

[16] Kelly Harrington, *Renewables, Reliability Drive New England Transmission Investment*, SNL Energy Power Daily Northeast, Jan. 5, 2009, at 1, 1.

wake of *Maine Public*, FERC has required settling parties who wish to bind non-parties to include language stating that the standard to be applied to non-party challenges will be the most stringent standard permitted by law. That dozens of settlements using that language have been filed since *Maine Public* is not evidence of "disarray." It is evidence that many settling parties either fail to perceive or are able to tolerate the "uncertainty" to which Petitioners object.

CONCLUSION

The Petition should be denied.

Respectfully submitted,

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AMICUS CURIAE BRIEF

(2)

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No. 08-674

In the
Supreme Court of the United States

NRG POWER MARKETING, LLC, ET AL.,

PETITIONERS,

v.

MAINE PUBLIC UTILITIES COMMISSION, ET AL.,

RESPONDENTS.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF THE ELECTRIC POWER SUPPLY ASSOCIATION, COLORADO INDEPENDENT ENERGY ASSOCIATION, ELECTRIC POWER GENERATION ASSOCIATION, INDEPENDENT POWER PRODUCERS OF NEW YORK, NATURAL GAS SUPPLY ASSOCIATION, NEW ENGLAND POWER GENERATORS ASSOCIATION, INC., NORTHWEST & INTERMOUNTAIN POWER PRODUCERS COALITION, AND WESTERN POWER TRADING FORUM AS *AMICI CURIAE* IN SUPPORT OF THE PETITION FOR CERTIORARI

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QUESTION PRESENTED

This Court's decision last Term in *Morgan Stanley Capital Group Inc. v. Public Utility District No. 1 of Snohomish County*, 128 S. Ct. 2733 (2008) reaffirmed that, under the *Mobile-Sierra* doctrine, the Federal Energy Regulatory Commission "must presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law," and that the "presumption may be overcome only if" the Commission "concludes that the contract seriously harms the public interest." *Id.* at 2737. In conflict with *Morgan Stanley* and decisions of other courts of appeals, the D.C. Circuit below held that "when a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply." Pet. App. 22a.

The question presented is:

Whether the Commission's authority to abrogate freely negotiated wholesale power contracts is constrained by the *Mobile-Sierra* doctrine when a contract rate is challenged by a non-contracting third party.

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INTEREST OF *AMICI CURIAE*[1]

Amici and their members represent a diverse array of participants in the Nation's electric and natural gas industries that are directly affected by the issues raised in this case. *Amici*'s members have made long-term financial commitments, involving hundreds of billions of dollars, in reliance on this Court's settled authorities protecting the integrity of privately negotiated wholesale power contracts. Because the D.C. Circuit's decision undoes much of this Court's work in *Morgan Stanley Capital Group Inc. v. Public Utility District No. 1 of Snohomish County*, 128 S. Ct. 2733 (2008), and purports to grant the Federal Energy Regulatory Commission never-before-recognized authority to abrogate contracts challenged by non-contracting third parties, *amici* are concerned that, if left standing, the decision below will destabilize the Nation's power markets, discourage much-needed investment, and ultimately lead to higher costs for consumers.

The Electric Power Supply Association **("EPSA").** EPSA is a national trade association representing competitive electric power suppliers, including independent power producers, merchant

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[1] The parties have consented to the filing of this brief in letters on file in the Clerk's office. Pursuant to S. Ct. R. 37.6, *amici* state that no counsel for any party authored this brief in whole or in part, and no person or entity, other than *amici* and its counsel, made a monetary contribution intended to fund the preparation or submission of this brief. More than ten days prior to the due date, *amici* provided counsel of record for all parties with notice of their intent to file this brief.

generators, and power marketers. EPSA's mission is to promote legislative and regulatory policies encouraging a competitive market for electricity.

Colorado Independent Energy Association **("CIEA").** CIEA is a trade association of competitive independent power producers operating in Colorado. Its 34 members and 12 associate members are an integral part of Colorado's energy industry, producing electricity with clean, efficient natural gas-fired cogeneration and renewable technologies.

Electric Power Generation Association **("EPGA").** EPGA is a regional trade association of major electric generating companies that supply wholesale power in Pennsylvania and surrounding states. Its member companies collectively own and operate more than 141,000 megawatts of generating capacity, approximately half of which is located in the mid-Atlantic region.

Independent Power Producers of New York **("IPPNY").** IPPNY is a not for profit trade association representing more than 100 independent power producers involved in the development of generation, marketing, and sale of electric power and natural gas in the state of New York.

Natural Gas Supply Association **("NGSA").** NGSA is a trade association that represents U.S.-based producers and marketers of natural gas on issues that broadly affect the natural gas industry. NGSA is the voice of suppliers who find, sell, transport, and deliver approximately 30 percent of the United States' natural gas supply. Established

in 1965, NGSA encourages the use of natural gas within a balanced national energy policy and promotes the benefits of competitive markets to ensure reliable and efficient transportation and delivery of natural gas and to increase the supply of natural gas to U.S. consumers.

New England Power Generators Association, Inc. **("NEPGA").** NEPGA is a trade association representing electric generating companies in New England. Its member companies account for approximately 26,000 megawatts of generating capacity in the region.

Northwest & Intermountain Power Producers Coalition **("NIPPC").** NIPPC represents developers, owners, and operators of non utility power plants in the Pacific Northwest and Intermountain region.

Western Power Trading Forum **("WPTF").** WPTF is a California non-profit, mutual benefit corporation. It is a broadly based membership organization dedicated to enhancing competition in Western electric markets in order to reduce the cost of electricity to consumers throughout the region while maintaining the current high level of system reliability. WPTF's actions are focused on supporting development of competitive electricity markets throughout the region and developing uniform operating rules to facilitate transactions among market participants.

INTRODUCTION

This Court has long recognized, and reaffirmed just last summer, that the Commission has no authority to modify voluntarily negotiated, fixed-price bulk energy contracts, except in "extraordinary circumstances" where revising contract terms is "necessary in the public interest." *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332, 344 (1956); *Morgan Stanley Capital Group Inc. v. Public Util. Dist. No. 1 of Snohomish County*, 128 S. Ct. 2733, 2737 (2008). This constraint on Commission authority serves a "reasonable accommodation between the conflicting interests of contract stability on the one hand and public regulation on the other." *Mobile*, 350 U.S. at 344. It also promotes a flexible, stable, and reliable regulatory regime.

Regulatory certainty, including the assurance that contracts for Commission-jurisdictional services are protected from modification, has played a central role in the development of the Nation's bulk power markets. The ability to enter into long-term contracts has provided market participants with an essential tool for hedging against future market fluctuations. In the Commission's expert judgment, "[c]ompetitive power markets simply cannot attract the capital needed to build adequate generating infrastructure without regulatory certainty, including certainty that the Commission will not modify market-based contracts unless there are extraordinary circumstances." *Nevada Power Co. v. Duke Energy*

Trading & Mktg., LLC, 99 FERC ¶ 61,047, at 61,190 (2002).

The D.C. Circuit's decision below—which fashions a new test for modifying contracts challenged by non-contracting third parties—threatens to upend the balance struck by Congress in the Federal Power Act and affirmed by this Court in *Morgan Stanley*. If allowed to stand, the decision below risks destabilizing the Nation's wholesale energy markets and infecting those markets with legal uncertainty at a particularly critical juncture.

REASONS FOR GRANTING THE WRIT

The Court should grant review for the same reasons it granted review in *Morgan Stanley*. This Court's intervention is also needed to preserve the practical impact of its judgment in *Morgan Stanley*: to correct the D.C. Circuit's unwise judicial policymaking in an industry of central national importance; and to resolve the gap between the D.C. Circuit's decision and decisions of other courts of appeals. If not corrected, the decision below threatens to unsettle contract stability and inhibit much-needed investment in the Nation's bulk power markets.

A. The Court Should Grant Review For The Same Reasons It Granted Review In *Morgan Stanley*.

Over a half-century ago, in two unanimous decisions referred to collectively as *Mobile-Sierra*, this Court held that the Federal Power Act preserves the integrity of private contracts. *See*

United Gas Pipe Line Co. v. Mobile Gas Serv. Corp., 350 U.S. 332, 344 (1956); *Federal Power Comm'n v. Sierra Pac. Power Co.*, 350 U.S. 348 (1956). The decisions recognize that when parties freely negotiate a wholesale energy contract, the agreed-on rates are presumptively "just and reasonable," as required under the Federal Power Act, and the contract may not be abrogated except in "extraordinary circumstances" of "unequivocal public necessity." *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 822 (1968).

Last Term, this Court affirmed the *Mobile-Sierra* doctrine's continuing vitality in *Morgan Stanley Capital Group Inc. v. Public Utility District No. 1 of Snohomish County*, 128 S. Ct. 2733 (2008). Reversing Ninth Circuit decisions that threatened "disfigurement of the venerable" doctrine, *id.* at 2747, the Court reiterated that a "rate set out in a freely negotiated wholesale-energy contract" is presumed to satisfy "the 'just and reasonable' requirement imposed by law." *Id.* at 2737. Holding that the Commission "may abrogate a valid contract only if it harms the public interest," *id.* at 2747, the Court emphasized that contract stability "ultimately benefits" the broader public because "uncertainties regarding rate stability and contract sanctity can have a chilling effect on investment and a seller's willingness to enter into long-term contracts," which "in the long run" will "harm consumers." *Id.* at 2749 (quotation and citation omitted). Accordingly, because "[t]he regulatory system created" by the Federal Power Act is "premised on contractual agreements voluntarily devised by the regulated companies; it

contemplates abrogation of these agreements only in circumstances of unequivocal public necessity." *Id.* at 2739 (quoting *Permian*, 350 U.S. at 822).

Morgan Stanley should have prompted the D.C. Circuit to revisit its decision carving out a substantial new exception to the *Mobile-Sierra* doctrine. Instead, the court of appeals held that *Mobile-Sierra* is designed merely to "preserve the terms of the bargain as between the contracting parties" and "simply does *not* apply" when a "rate challenge is brought by a non-contracting third party." Pet. App. 22a (emphasis added). In the D.C. Circuit's view, *Mobile-Sierra* serves the limited purpose of "mak[ing] it more difficult for either party to shirk its contractual obligations," but has no application when a contract is challenged by a non-party. *Id.* (emphasis in original).

If left uncorrected, the D.C. Circuit's decision will have dramatic, far-reaching consequences for the Nation's energy markets. Like the Ninth Circuit decisions in *Morgan Stanley*, the decision below threatens contract stability and will inhibit much-needed investment in energy infrastructure. In the energy industry, contract stability is crucial because investors are loath to invest in highly volatile, hard-to-predict power markets unless they can rely on the sanctity of long-term, fixed-price contracts. *See* CERA Advisory Services, *California Power Crisis Aftershock: The Potential Modification of Western Power Contracts*, at 5-6 (Apr. 2007) ("*Aftershock*"), available at http://www2.cera.com/westernpowercontracts; The Electric Energy Market Competition Task Force, *Report to Congress*

on Competition in Wholesale and Retail Markets for Electric Energy, at 4 (Apr. 2007) (long-term contracts are "critical in obtaining financing for new generation and ensuring adequate supplies for retail loads at predictable prices"). From an investor's perspective, it makes no difference whether a contract is subject to challenge by a disgruntled contracting party or by a "non-contracting third party." Pet. App. 22a. The D.C. Circuit's newly fashioned exception to *Mobile-Sierra* thus casts a pall of uncertainty over future investments in the Nation's bulk power markets, calling into question the very rules and practices governing energy transactions that *Morgan Stanley* reaffirmed.

It bears emphasis that, in contrast to standing requirements that might apply to disputes involving ordinary commercial contracts, *cf. Miree v. DeKalb County, Ga.*, 433 U.S. 25 (1977) (state law applies to determine whether third party beneficiaries enjoy standing), the Federal Power Act's permissive standing requirements allow virtually anyone to file a complaint with the Commission challenging an energy contract as unjust, unreasonable, or unduly discriminatory. *See* 16 U.S.C. § 825e (2000 & Supp. V 2005) ("[a]ny person ... complaining of anything done ... by any ... public utility ... may apply to the Commission by petition"). As the Commission's regulations state, "*[a]ny person* may file a complaint seeking Commission action against any other person alleged to be in contravention or violation of any statute, rule, order, or other law administered by the Commission, or for any alleged wrong over

which the Commission may have jurisdiction." 18 C.F.R. § 385.206(a) (2008) (emphasis added); *see also Panhandle Complainants v. Southwest Gas Storage Co.*, 117 FERC ¶ 61,318 at ¶ 21 & n.22 (2006) (rejecting challenges to parties' standing). Those permissive rules reflect the reality that the regulatory regime simply does not admit of the strict dichotomy between contracting and non-contracting parties assumed by the court below.

The upshot is that third parties routinely file complaints with the Commission seeking to re-write energy contracts on grounds that the contract rates are either too high or too low and, therefore, not "just and reasonable." For example, last year, a consumer group filed complaints challenging a series of freely negotiated contracts between utilities and energy suppliers in California. *See* Section 206 Compl., FERC Dkt. No. EL07-50-000 (Mar. 26, 2007) (challenging contract between Southern California Edison Co. and Blythe Energy, LLC); Section 206 Compl., FERC Dkt. No. EL7-40-000 (Mar. 2, 2007) (challenging contract between Pacific Gas & Electric Co. and Metcalf Energy Center and Los Medanos Energy Center, LLC); Section 206 Compl., FERC Dkt. No. EL07-37-000 (Feb. 22, 2007), available at http://elibrary.ferc.gov. Similarly, the Illinois Attorney General filed a complaint seeking to abrogate freely negotiated contracts between Illinois utilities and 16 wholesale suppliers that she alleged would lead to excessive charges on Illinois consumers. *See Amended Compl. by the People of the State of Illinois, Ex Rel. Illinois Attorney General Lisa Madigan*, Docket No.

EL07-47-000 (Mar. 16, 2007), available at http://elibrary.ferc.gov.

Because long-term wholesale energy contracts affect (either directly or indirectly) not only the sophisticated parties who negotiate them but also numerous third parties, there is no shortage of state regulators, consumer advocacy groups, retail consumers, industrial buyers, upstream suppliers, and other interested stakeholders available to take advantage of the Commission's permissive rules for challenging contract rates. *See* Pet. 21. Indeed, in *Morgan Stanley* itself, a long line of third parties stood ready to challenge the parties' contracts as imposing an "excessive burden." *Morgan Stanley*, 128 S. Ct. at 2747 (rejecting the Ninth Circuit's "excessive burden" exception to *Mobile-Sierra*). (As Petitioners note, one of the respondents in *Morgan Stanley*, the Office of the Nevada Attorney General, was not a party to the underlying contracts. *See* Pet. 21.) Allowing those suits to proceed would just as surely undermine "contract stability as between the contracting parties," Pet. App. 24a, as would permitting a party to complain about contract rates to which it voluntarily agreed. *Morgan Stanley*, 128 S. Ct. at 2747. In either instance, changing the contract rate, absent a compelling public interest, would "threaten to inject more volatility into the electricity market by undermining a key source of stability." *Id.* at 2749.

The timing of the D.C. Circuit's assault on *Mobile-Sierra* could not be more inauspicious. The power sector requires hundreds of billions of dollars in investment in order to meet growing demand and to address environmental concerns. *See* The

Brattle Group, *Transforming America's Power Industry: The Investment Challenge*, at 4 (Apr. 21, 2008) (estimating that, even with substantial efficiency improvements, the U.S. power sector will require 150,000 MW of new and replacement generation plants at an approximate cost of $560 billion), available at http://www.Edisonfoundation.net; *Aftershock*, at 16 (increasing demand will require at least "$400 billion in investment in new and existing power plants"). At the same time, well-documented turmoil in capital and credit markets has increased the cost and difficulty of attracting investment. It is precisely in these circumstances where "the integrity of contractual relations is an interest of paramount importance." *Local 926 Int'l Union of Operating Eng'rs, AFL-CIO v. Jones*, 460 U.S. 669, 687 n.4 (1983). As economists have long recognized, contract stability is important in promoting economic development, "especially with respect to economic regulation of capital-intensive industries, such as the electric and natural gas industries." Richard P. Bress, et al., *A Deal Is Still A Deal: Morgan Stanley Capital Group v. Public Util. Dist. No. 1*, 2008 Cato Supreme Court Review 285, 285-86 n.2.

At bottom, then, this Court's review is needed for the same reasons it was needed in *Morgan Stanley*—to prevent lasting damage to the Nation's wholesale energy markets. If not corrected, the D.C. Circuit's new exception will gut *Morgan Stanley*, effectively consigning that decision and the *Mobile-Sierra* doctrine to a footnote in the regulation of the energy industry. It also will upend the stability of long-term contracts on which

this Nation's energy markets depend. The lower court's disruptive decision should not be allowed to stand.

B. The Decision Below Conflicts With *Morgan Stanley*.

The decision below merits this Court's review for all the same reasons review was appropriate in *Morgan Stanley*, plus one additional, new reason: the Court should grant *certiorari* to vindicate its *Morgan Stanley* decision. As Petitioners' explain in more detail, the lower court's decision cannot be reconciled with *Morgan Stanley* and the foundational energy law principles it recognizes.

The decision below rests on the D.C. Circuit's view that *Mobile-Sierra* is a narrow "exception" to the statutory requirement that rates be "just and reasonable." The court of appeals thus reasoned that *Mobile-Sierra* "carves out an exception" to the rule that contract rates must satisfy the "'just and reasonable' standard" required under the Federal Power Act. Pet. App. 20a. The D.C. Circuit concluded that *Mobile-Sierra* does not apply when a contract rate is challenged by a non-contracting third party, because applying *Mobile-Sierra* would deprive that party of its "statutory right to have rate challenges adjudicated under the 'just and reasonable' standard." *Id.* 22a. Relying on a case interpreting the Federal Arbitration Act, the D.C. Circuit noted that "'[i]t goes without saying that a contract cannot bind a nonparty.'" *Id.* (quoting *EEOC v. Waffle House, Inc.*, 534 U.S. 279, 294 (2002)).

That reasoning is deeply flawed. A contractually negotiated rate is not just an ordinary contract. Precisely because the contract rate remains a "rate," third parties have standing to challenge it under a much more permissive standard than would apply in an ordinary contract action.

Significantly, the Court in *Morgan Stanley* rejected the notion that contractually negotiated rates were a deviation from just-and-reasonable rate principles, giving no weight to "the obviously indefensible proposition that a standard different from the statutory just-and-reasonable standard applies to contract rates." *Morgan Stanley*, 128 S. Ct. at 2740. To the contrary, because wholesale energy contracts are typically negotiated between sophisticated entities enjoying equal bargaining power, the negotiated rate is expected to be, and by definition constitutes, a "just and reasonable" rate. *Id.* at 2746 (citing *Verizon Commc'ns, Inc. v. FCC*, 535 U.S. 467, 479 (2002)). The *Mobile-Sierra* doctrine is not, as the D.C. Circuit assumed, an "exception" to the just-and-reasonable standard; instead, it is a "definition of what it means for a rate to satisfy" that standard in the contract context. *Id.* In short, *Mobile-Sierra*'s "'public interest standard' refers to the differing *application*" of the "just-and-reasonable standard to contract rates." *Id.* (emphasis in original)

Moreover, applying the *Mobile-Sierra* doctrine to contract rates, regardless of who may challenge them, does *not* deprive any party of their statutory rights. The Federal Power Act's "just and reasonable" standard is properly viewed not as a

right granted to parties, but as a constraint on the Commission's authority, framing the boundaries of Commission action. The Court has thus recognized that the Federal Power Act ensures that when a contract is freely negotiated between sophisticated parties, the contract rate is presumed to satisfy the statutory standard, except in "extraordinary circumstances where the public will be severely harmed." *Morgan Stanley*, 128 S. Ct. at 2749. Contrary to the conclusions reached by the court below, a just and reasonable contract rate does not lose that quality merely because it is challenged by a non-contracting third party.

In addition to taking an approach at odds with *Morgan Stanley*, the D.C. Circuit's decision cannot be reconciled with the Federal Power Act's settled policies favoring freedom of contract. As *Morgan Stanley* recognized, contracting parties are free to select by contract the standard of review to be applied by the Commission. Absent any indication to the contrary, *Mobile-Sierra*'s "default rule" will apply, ensuring the agreed-on contract rate is protected unless it "seriously harms the consuming public." *Id.* at 2746. Alternatively, however, the contracting parties may opt out of the *Mobile-Sierra* presumption by including in their contracts what is known as a *Memphis* clause, after this Court's decision in *United Gas Pipe Line Co. v. Memphis Light, Gas & Water Div.*, 358 U.S. 103 (1958). *See Morgan Stanley*, 128 S. Ct. at 2739. Finally, as a third alternative, the contracting parties may agree on a "middle option" in the form of a contract "that does not allow the seller to supersede the contract rate by filing a new rate,"

but does "permit the Commission to set aside the contract rate if it results in an unfair rate of return, not just if it violates the public interest." *Id.*

This menu of regulatory options makes no sense if, as the D.C. Circuit held, the *Mobile-Sierra* doctrine "does not apply" when a contract rate is challenged by a "non-contracting third party." Pet. App. 22a. To the contrary, under the D.C. Circuit's approach, the "*Mobile-Sierra* presumption" will cease to be the "default rule." *Morgan Stanley*, 128 S. Ct. at 2746. Instead, as a practical matter, because non-contracting third parties can be expected to challenge virtually any contract under the Federal Power Act, every contract would become presumptively subject to the Commission's ongoing authority to order modifications whenever a rate of return is arguably too high or too low. Nor would there be any reason for a seller to negotiate for the "middle option" if review under the ordinary just and reasonable standard could be obtained through the simple expedient of finding a non-contracting third party to challenge the contract rate. In the end, then, if allowed to stand, the D.C. Circuit's decision will strip contracting parties' of their heretofore "broad authority" to structure their agreements as they see fit, nullifying the freedom of contract promoted by "decisions of this Court and the Courts of Appeals" for "the past 50 years." *Morgan Stanley*, 128 S. Ct. at 2739.

C. The Decision Below Conflicts With Decisions From Other Courts Of Appeals.

By inventing a new test that creates a gaping exception to *Mobile-Sierra* whenever a non-contracting third party challenges a contract, the D.C. Circuit's decision has opened a conflict with decisions of other courts of appeals. The Court should grant review to close this conflict and restore the settled understandings of the Federal Power Act by which market participants, like *amici*'s members, have negotiated contracts and ordered their affairs.

In the proceedings below, the Commission correctly observed that "there is no Commission or court precedent that supports a finding that a non-signatory may unilaterally seek changes to a *Mobile-Sierra* 'public interest' contract" under a different, broader notion of "the 'just and reasonable' standard of review." Pet. App. 23a (citing *Devon Power LLC*, 115 FERC ¶ 61,340 at 62,335 (2006)). Brushing aside this precedent, the D.C. Circuit criticized the Commission for applying an "illegal standard." *Id.* According to the D.C. Circuit, "it could just as easily be said that there is no 'court precedent' that supports altering third parties' statutory rights based on a contract that they refuse to sign." *Id.* That blithe assertion misses the point.

The Commission has consistently held that the *Mobile-Sierra* doctrine applies equally to party and non-party challenges to contract rates. *See* Pet. App. 23a (acknowledging that the Commission's

policy in this regard has been consistent since 2002). Although these decisions have not been tested on review, the Commission's consistent approach is powerful evidence of what had been thought to be settled rules and understandings governing wholesale power transactions. *See California v. FERC*, 495 U.S. 490, 499 (1990) (recognizing the respect "this Court must accord to longstanding and well-entrenched decisions, especially those interpreting statutes that underlie complex regulatory regimes"). The fact that no court has expressly addressed the precise issue does not mean the D.C. Circuit was painting on a blank canvas when it considered *Mobile-Sierra*'s applicability to non-contracting third parties.

The decision below is at odds with the First Circuit's decisions in two cases concerning Commission-ordered modifications to a power contract between a supplier and its prospective affiliate. *See Northeast Utils. Serv. Co. v. FERC*, 993 F.2d 937 (1st Cir. 1993) ("*NUSCO I*"); *Northeast Utils. Serv. Co. v. FERC*, 55 F.3d 686 (1st Cir. 1995) ("*NUSCO II*"). In *NUSCO I*, the First Circuit held that the Commission improperly "circumvent[ed] the *Mobile-Sierra* doctrine," because it ordered contract modifications without first determining whether the modifications were compelled by the public interest. *NUSCO I*, 993 F.2d at 961. Given the relationship between the two parties, whose interests were aligned, the Commission was not resolving a challenge brought by one of the parties to the contract, but instead responding to a protest filed by a non-contracting third party. *See Northeast Utils. Serv. Co.*, 50

FERC ¶ 61,266 at 61,831-32 (1990) (noting the protest filed by the Massachusetts Wholesale Electric Company). In *NUSCO II*, the First Circuit affirmed the Commission's order on remand, holding that in further proceedings the Commission had properly applied the *Mobile-Sierra* doctrine.

Although the Commission in the *NUSCO* proceedings ordered the contract modified on its own initiative, without relying on arguments pressed by the third party, the fact remains that the First Circuit recognized that *Mobile-Sierra* served principally as a constraint on the *Commission*'s authority to modify contract rates. The statutory standard was not a "right" to be granted to, or waived by, the non-contracting party, but a limit on the agency's ability to interfere with contracts. *Cf.* Pet. App. 23a n.9 (holding that Commission oversight "does not justify the derogation of the statutory right to 'just and reasonable' review of rates"). The First Circuit's *NUSCO* decisions are thus squarely in conflict with the D.C. Circuit's decision below.

The *NUSCO* decisions also spotlight how badly the D.C. Circuit has misapprehended *Mobile-Sierra*'s effect on the Commission's ability to protect the interests of third parties. In *NUSCO*, the Commission required contract modifications because the "negotiated" rates, set by parties whose interests were closely aligned, would inure to the detriment of "non-parties to the contract." *NUSCO II*, 55 F.3d at 692. Nothing prevented the Commission from taking appropriate action to order the contract modified. As this Court recognized over fifty years ago, the *Mobile-Sierra*

presumption "in no way impairs the regulatory powers of the Commission" because jurisdictional "contracts remain fully subject to the paramount power of the Commission to modify them when necessary in the public interest." *Mobile*, 350 U.S. at 344. The Commission has "plenary authority to limit or to proscribe contractual arrangements that contravene the relevant public interests." *Permian*, 390 U.S. at 784.

Finally, as Petitioners emphasize, in addition to creating a split among the Circuits, the decision below has "created disarray" in the industry, with the Commission adopting a new, nationwide policy that contracts subject to *Mobile-Sierra* will impose on "non-contracting third parties the most stringent standard permissible under applicable law." Pet. 22 (citing *Duke Energy Carolinas, LLC*, 123 FERC ¶ 61,201, at 62,290 n.10 (2008)). Any change in legal regimes that acts, as does the D.C. Circuit's decision, to replace settled rules with this kind of vague administrative directive necessarily opens the door to arbitrary agency decisionmaking.

Having now "bargain[ed] in the shadow" of *Mobile-Sierra* for more than five decades, *Boston Edison Co. v. FERC*, 233 F.3d 60, 66 (1st Cir. 2000), energy market participants have ordered their affairs on the assumption that the Commission will modify contracts only in accordance with *Mobile-Sierra*'s well-defined understanding of "extraordinary circumstances" of "unequivocal public necessity." *Permian*, 390 U.S. at 820-22. Upsetting those expectations not only engenders uncertainty, it invites an interlude of impossible-to-predict agency reaction. The risk

that market participants will be unnecessarily subject to uncertain Commission policies poses an undeniable further threat to the stability of our Nation's energy markets at the worst possible juncture. That threat can and should be defused by this Court's review of the decision below.

CONCLUSION

For the foregoing reasons, the Court should grant a writ of *certiorari*.

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JOINT APPENDIX

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IN THE

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NRG POWER MARKETING, LLC, *ET AL.*,
Petitioners,

v.

MAINE PUBLIC UTILITIES COMMISSION, *ET AL.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

JOINT APPENDIX

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BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Docket No. ER03-563

IN RE DEVON POWER LLC

RELEVANT DOCKET ENTRIES

DATE	PROCEEDINGS
02/26/2003	Devon Power LLC et al submits [ ] Cost-of-Service Agreements among PMI & ISO New England, Inc under ER03-563.
	* * * * *
04/25/2003	Order accepting, in part, requests for reliability must-run contracts & directing temporary bidding rules re Devon Power LLC under ER03-563.
	* * * * *
07/24/2003	Order on rehearing & compliance re Devon Power Co et al under ER03-563.
	* * * * *
03/01/2004	ISO New England Inc submits its filing in compliance with FERC's directive of 4/25/03 under ER03-563.

DATE	PROCEEDINGS
	* * * * *
06/02/2004	Order on compliance filing & establishing hearing procedures re Devon Power LLC, with Commissioner Kelliher concur[r]ing statement attached & Commissioner Kelly not participating under ER03-563 et al.
	* * * * *
11/08/2004	Order on rehearing of FERC's 6/2/04 Order and clarification re Devon Power LLC et al under ER03-563 et al.
11/08/2004	Order on ISO New England Inc's 7/2/04 compliance filing re Devon Power LLC under ER03-563 et al.
	* * * * *
12/03/2004	Order confirm[i]ng rulings re Devon Power LLC under ER03-563.
	* * * * *
02/23/2005	Exhibit ISO-17 in Devon Power, LLC's proceeding under ER03-563: Direct Testimony of Steven E Stoft.
	* * * * *
03/03/2005	Exhibit ISO-3 in Devon Power, LLC's proceeding under ER03-563: Questions & Answers re John J Reed's testimony on behalf of ISO New England, Inc.
	* * * * *

DATE	PROCEEDINGS
03/08/2005	Exhibit ISO-1 in Devon Power, LLC's proceeding under ER03-563: Direct Testimony of David LaPlante.
	* * * * *
03/08/2005	Exhibit ISO-23 in Devon Power LLC's proceeding under ER03-563: Rebuttal Testimony of David LaPlante.
	* * * * *
03/23/2005	Order on rehearing and clarification on FERC's order issued 6/2/04 re Devon Power LLC w/Commissioner Kelly not participating under ER03-563 et al.
03/23/2005	Order on rehearing on FERC's order issued 6/2/04 re Devon Power LLC w/Commissioner Kelly not participating under ER03-563 et al.
	* * * * *
03/24/2005	Exhibit MV-1 in Devon Power, LLC's proceeding under ER03-563: Prepared direct testimony and accompanying exhibits of Thomas Austin.
	* * * * *
06/15/2005	Initial Decision regarding Devon Power LLC, et al under ER03-563.
	* * * * *

DATE	PROCEEDINGS
07/15/2005	Brief on Exceptions of the Maine Public Utilities Commission, the Maine Public Advocate, the Vermont Department of Public Service and the Vermont Public Service Board under ER03-563.
07/15/2005	The Connecticut Parties Request for Oral Argument in docket ER03-563.
	* * * * *
07/15/2005	Brief on Exceptions of New England Conference of Public Utilities Commissioners under ER03-563.
	* * * * *
07/28/2005	Motion of New England Conference of Public Utilities Commissioners, et al. for Oral Argument under ER03-563.
	* * * * *
08/04/2005	Brief Opposing Exceptions of ISO New England Inc. under ER03-563.
	* * * * *
08/10/2005	Order granting oral argument and delaying implementation of locational installed capacity mechanism re Devon Power, LLC et al with Commissioner Brownell concurring statement attached under ER03-563.
	* * * * *
08/25/2005	Notice scheduling oral argument re Devon Power LLC under ER03-563.
	* * * * *

DATE	PROCEEDINGS
09/13/2005	Proposal of Maine PUC, VTPSB, NHPSC and RIPUC under ER03-563.
	* * * * *
09/14/2005	Errata to the Notice of Proposed Speakers and Time Allocation for Oral Argument of ISO NEW ENGLAND INC under ER03-563.
	* * * * *
09/20/2005	Transcript of 9/20/05 oral argument at FERC regarding Devon Power LLC et al under ER03-563.
	* * * * *
10/07/2005	Joint Motion to Appoint Settlement Judge and Request for Expedited Response and Consideration under ER03-563-030.
	* * * * *
10/21/2005	Interim Order regarding settlement procedures & directing compliance filing re Devon Power, LLC under ER03-563.
10/21/2005	Order of Chief Judge designating Settlement Judge re Devon Power, LLC under ER03-563.
	* * * * *
11/18/2005	Report by Settlement Judge regarding Devon Power LLC, et al under ER03-563.
	* * * * *

DATE	PROCEEDINGS
12/19/2005	Report by Settlement Judge to the Chief Judge and the Commission re Devon Power LLC under ER03-563.
	* * * * *
01/23/2006	Report by Settlement Judge re Devon Power, LLC under ER03-563.
	* * * * *
01/31/2006	Report by Settlement Judge re Devon Power, LLC et al under ER03-563.
	* * * * *
03/06/2006	ISO New England, Inc submits an explanatory statement in support of settlement agreement of the settling parties and request for expedited consideration and settlement agreement resolving all issues etc under ER03-563 et al.
	* * * * *
03/07/2006	ISO New England Inc submits a corrected table of contents for the Settlement Agreement, corrected listings of the Settling Parties for the Explanatory Statement in Support of the Settlement Agreement et al under ER03-563.
03/10/2006	Order scheduling settlement comments re Devon Power LLC et al under ER03-563.
03/27/2006	Settlement Comments of Berkshire Power Company, LLC In Support of Settlement under ER03-563, et al.

DATE	PROCEEDINGS
03/27/2006	Comments of CONSOLIDATED EDISON ENERGY, INC. in support of Settlement Agreement under ER03-563.
03/27/2006	Settlement Comments of EnerNOC, Inc re Devon Power, LLC et al under ER03-563.
03/27/2006	Settlement Comment of Exelon Corporation under ER03-563.
03/27/2006	Settlement Comments in Support of Settlement Agreement of Select Energy, Inc. under ER03-563.
03/27/2006	Settlement Comments of the Industrial Energy Consumer Group under ER03-563.
03/27/2006	Settlement Comments of the CT DPUC, CT OCC, CL & P, NH PUC, RI PUC, RI Div. of Pub. Util. & Carriers, VPSB, VDPS under ER03-563.
03/27/2006	Initial Comments of the PPL Parties on Settlement under ER03-563, et al.
03/27/2006	Settlement Comment of LIPA under ER03-563.
03/27/2006	Comments of PSEG Energy Resources & Trade LLC on Settlement Agreement under ER03-563-000, et al.
03/27/2006	Comments in Opposition to Settlement by NSTAR Electric & Gas Corporation, et al.
03/27/2006	Supplemental Comments of NSTAR Electric & Gas Corporation in Opposition to Settlement under ER03-563, et al.

DATE	PROCEEDINGS
03/27/2006	Settlement Comment of State of Maine Public Utilities Commission, et al. under ER03-563, et al.
03/27/2006	Settlement Comments of Reading Municipal Light Department under ER03-563, et al.
03/28/2006	Load Supporters submits the affidavit of Dr Miles Bidwell for its Initial Comments in Support of Offer of Settlement re Devon Power LLC et al under ER03-563.
03/31/2006	Harkins Cunningham LLP submits the notarized signature page of Thomas D Austin, to the Affidavit submitted as an attachment to the comments filed 3/27/06 re Devon Power LLC et al under ER03-563.
03/31/2006	Erving Paper Mills, Inc addresses the proposed Locational Installed Capacity implementation, as well as the usage of Demand Response Programs in the electrical market, which directly affects Erving Paper Mill etc under ER03-563.
04/05/2006	Reply Comments of National Grid USA under ER03-563. (Replacement for 20060405-5059).
04/05/2006	Reply Comments of the CT DPUC, CT OCC, NH PUC, RI PUC, RI Div. of Pub. Util. & Carriers, VT PSB, VT DPS, PSC of NH, and CT L & P under ER03-563. (replacement for 20060405-5062)
04/05/2006	Comments of Calpine Energy Services, L.P. under ER03-563.
04/05/2006	Reply of Milford Power Company, LLC under ER03-563.

DATE	PROCEEDINGS
04/05/2006	Reply Comments of Lake Road Generating Company, L.P. and Granite Ridge Energy, LLC in Support of Settlement under ER03-563.
04/05/2006	Reply Comments of American National Power, Granite Ridge Energy and TransCanada Power Marketing to Comments Opposing Proposed Settlement in ER03-563.
04/05/2006	Settlement Reply Comment of ISO New England Inc. under ER03-563.
04/05/2006	Reply Comments of the PPL Parties on Settlement under ER03-563.
04/05/2006	Settlement Reply Comments of Massachusetts Municipal Wholesale Electric Company and Reading Municipal Light Department, under ER03-563.
04/05/2006	Settlement Reply Comments of Connecticut Municipal Electric Energy Cooperative, under ER03-563.
04/05/2006	Reply Comments of New York Independent System Operator, Inc. under ER03-563.
04/05/2006	Reply Comments of NEPOOL Participants Committee in support of Offer of Settlement in Docket No. ER03-563.
04/05/2006	Reply Comments of CAPACITY SUPPLIERS in support of settlement re Devon Power LLC, et al under ER03-563, et al.
04/05/2006	Reply Comments of Objecting Parties to initial comments in support of settlement re Devon Power, LLC et al under ER03-563.

DATE	PROCEEDINGS
04/05/2006	Comments of The Maine Public Utilities Commission And The Maine Public Advocate In Reply To Comments Supporting The Proposed Settlement under ER03-563, et al.
04/06/2007	NRG Companies Reply to Comments in Opposition to Settlement under ER03-533, et al.
04/06/2006	Errata Comments to Filing of NRG Companies under ER03-563.
04/11/2006	Report on Contested Settlement by Settlement Judge re Devon Power LLC under ER03-563.
04/11/2006	Report on contested settlement by Settlement Judge Lawrence Brenner re Devon Power LLC, et al under ER03-563. (This replaces 20060411- 3060)
04/11/2006	Comments of Exelon Corporation under ER03-563.
04/11/2006	Maine Public Util[i]ties Commission et al submits two pages of Page 6 to be substituted in the Supplemental Aff[i]davit of Thomas D Austin to the reply comments that it submitted electronically on 4/5/06 under ER03-563.
	* * * * *
04/14/2006	Order of Chief Judge terminating Settlement Judge procedures regarding Devon Power LLC, et al under ER03-563.
	* * * * *

DATE	PROCEEDINGS
05/03/2006	Supplement to report on contested Settlement by Settlement Judge re Devon Power LLC under ER03-563.
05/03/2006	Supplement to report on Contested Settlement by Settlement Judge to the Commission re Dev[o]n Power LLC under ER03-563.
05/15/2006	Letter order accepting ISO New England, Inc's Compliance filing submitting report updating prog[r]ess made in the siting, permitting, and construction of transmission upgrades with the New England control areas under ER03-563.
	* * * * *
05/17/2006	Massachusetts Department of Telecommunications & Energy informs FERC that they continue[ ] to oppose the Settlement Agreement re Devon Power, LLC et al under ER03-563.
05/26/2006	Devon Power LLC submits its 8th compliance report under ER03-563 et al.
06/02/2006	Combined Notice of Filings #1, 6/2/2006: This notice contains information concerning multiple filings received by FERC.
06/06/2006	Motion to Intervene Out of Time and For Leave to File Limited Comments Out of Time and Comments of EPIC Merchant Energy, LP and Black Oak Energy, LLC et al. under ER03-563.

DATE	PROCEEDINGS
06/12/2006	ISO New England Inc submits i[t]s revised eighth compliance report updating progress made in the sitting, permitting and construction of transmission and generation upgrades re Devon Power LLC under ER03-563 et al.
06/15/2006	News Release: Commission accepts settlement designed to resolve reliab[i]lity issues in New England Region under ER03-563.
06/15/2006	Statement of Chairman Joseph T Kelliher at the 6/15/06 Open Commission Meeting regarding E-1: Devon Power LLC et al under ER03-563.
06/15/2006	Combined Notice of Filings #1, June 15, 2006: This notice contains information concerning multiple filings received by FERC.
06/16/2006	Order accepting proposed Settlement Agreement re Devon Power LLC with Commissioner Kelly's concurring statement attached under ER03-563.
06/28/2006	Comments of US Senator Olympia J Snowe et al expressing concerns with FERC's approval of a forward Capacity Market for the New England Market under ER03-563.
07/14/2006	Request for Rehearing of FERC's Order Issued 6/16/2006 of the Industrial Energy Consumer Group under ER03-563, et al.
07/17/2006	Application for Rehearing of FERC's Order Issued 6/16/2006 of the Atty Gen of the Commonwealth of Massachusetts, et al.

DATE	PROCEEDINGS
07/17/2006	Request for Rehearing or Appeal of FERC's Order Issued 6/16/2006 of the Maine Public Utilities Commission and the Maine Public Advocate under ER03-563, et al.
07/19/2006	Response to US Senator Olympia J Snowe's 6/22/06 letter concerning the FERC's recent order approving a settlement that will create a Forward Capacity Market in New England under ER03-563.
07/19/2006	Response to US senator Susan M Collins' 6/22/06 letter concerning the FERC's recent order approving a settlement that will create a Forward Capacity Market in New England under ER03-563.
07/31/2006	Motion to Answer Request for Rehearing and Answer by the Connecticut Department of Public Utility Control under ER03-563.
07/31/2006	Motion for Leave to Answer Requests for Rehearing and Answer of the New England Power Pool Participants Committee under ER03- 563.
08/01/2006	Motion for Leave to Answer, Answer, and Request for Expedited Consideration of ISO New England Inc. under ER03-563, et al.
	* * * * *
08/09/2006	Motion to Intervene Out of Time of Casco Bay Energy Company, LLC under ER03-563, et al.
08/09/2006	Motion to Intervene Out of Time of Bridgeport Energy, LLC under ER03-563, et al.

DATE	PROCEEDINGS
08/14/2006	Order granting rehearing of FERC's order issued 6/16/06 for further consideration re Devon Power LLC under ER03-563.
08/24/2006	Ninth Compliance Report of ISO New England Inc. under ER03-563, et al.
	* * * * *
08/29/2006	Combined Notice of Filings #1, August 29, 2006: This notice contains information concerning multiple filings received by FERC.
	* * * * *
09/08/2006	Procedural Motion of Maine Public Utilities Commission under ER03-563. Motion to lodge in support of request for rehearing.
09/08/2006	Answer of Connecticut Department of Public Utility Control, the New England Conference of Public Utilities Commissioners, et al Opposing ISO New England Inc.'s Motion for Relief from Reporting requirement, etc ER03-563.
10/31/2006	Order on rehearing of FERC's June 2, 2004 Order and clarification re Devon Power LLC with Commissioner Wellinghoff's and Commissioner Kelly's concurring statements attached under ER03-563.
11/01/2006	News Release – Commission denies rehearing of New England's plann[ ]ed capacity market; proposed tariff accepted under ER03-563 et al.
	* * * * *

DATE	PROCEEDINGS
04/05/2007	Motion for a Stay of Transition Pay[ ]ments by Richard Blumenthal, Attorney General for the State of Connecticut under ER03-563, et al
	* * * * *
04/19/2007	Motion to Intervene Out-of-Time of the FirstLight Parties under ER03-563.
04/20/2007	Answer of Milford Power Company, LLC to Motion for a Stay of Transition Payments by Richard Blumenthal, Attorney General for the State of Connecticut under ER03-563, et al.
04/20/2007	Answer of Capacity Suppliers in Opposition to Motion for Stay under ER03-563, et al.
04/20/2007	Opposition of the New England Power Pool Participants Committee and ISO New England Inc. to Motion for Stay in ER03-563, et al.
04/20/2007	The New England Power Pool (NEPOOL) Participants Committee submits their Opposition to Motion for Stay re Devon Power, LLC under ER03-563.
	* * * * *
05/17/2007	News Release – Commission Denies Stay in New England Forward Capacity Market Proceeding under ER03-563.
05/17/2007	Order denying stay re Devon Power LLC under ER03-563.
	* * * * *

DATE	PROCEEDINGS
07/20/2007	Supple[ ]ment to the Certified Index of the Record re Maine Public Utilities Commission, et al v FERC under ER03-563 et al.
	* * * * *
01/15/2009	Order on remand re Devon Power LLC under ER03-563. Concurrence in part by Commissioners Kelly and Wellinghoff.
01/15/2009	News – FERC Addresses Standard of Review in Court Remand under ER03-563.
02/17/2009	ISO New England, Inc et al submit[ ] their Compliance Statement re New England's capacity market design under ER03-563.
02/19/2009	Combined Notice of Filings, February 19, 2009: This notice contains information concerning multiple filings received by FERC.
03/26/2009	Letter order accepting Devon Power LLC's et al Fourth Revised Cost-of-Service Agreements under ER03-563.
04/14/2009	Letter order accepting ISO New England Inc's compliance statement on behalf of the signatories to the settlement agreement in this proceeding in order to comply with the Commission's January 15, 2009 order in this proceeding under ER03-563.
04/14/2009	Letter order accepting ISO New England, Inc's Compliance Report on Locational Scarcity Pricing under ER03-563 et al.

Docket No. ER06-1465

ISO NEW ENGLAND INC. AND
NEW ENGLAND POWER POOL

RELEVANT DOCKET ENTRIES

DATE	PROCEEDINGS
09/01/2006	ISO New England, Inc et al filing implementing the Transition Provisions of the Forward Capacity Market Settlement Agreement filed on 3/6/06 under ER06-1465.
	* * * * *
09/22/2006	Notice of Intervention and Protest of Maine Public Utilities Commission under ER06-1465.
	* * * * *
10/31/2006	Order accepting tariff sheets regarding ISO New England Inc. and New England Power Pool 9/1/06 filing under ER06-1465.
	* * * * *
04/13/2007	Order Denying Rehearing of the Commission's October 31, 2006 Order for the Maine Public Utilities Commission re ISO New England, Inc and New England Power Pool under ER06-1465.

IN THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

Docket No. 06-1403

MAINE PUBLIC UTILITIES COMMISSION,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent.

Docket No. 06-1427

RICHARD BLUMENTHAL, ATTORNEY GENERAL FOR THE STATE OF CONNECTICUT, AND MARTHA COAKLEY, ATTORNEY GENERAL FOR MASSACHUSETTS,
Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent.

Docket No. 07-1193

MAINE PUBLIC UTILITIES COMMISSION,
Petitioner,

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent.

RELEVANT DOCKET ENTRIES[1]

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[1] All docket entries are from No. 06-1403 except as noted.

DATE	PROCEEDINGS
12/12/2006	PETITION FOR REVIEW CASE docketed. Petition for Review filed by Petitioner ME Pub Util Cmsn. [1010674-1]
	* * * * *
12/29/2006	PETITION FOR REVIEW CASE docketed. Petition for Review filed by Petitioner Richard Blumenthal, Petitioner Thomas F. Reilly. [1014005-1] [filed in No. 06-1427]
	* * * * *
01/05/2007	MOTION filed (5 copies) (certificate of service dated 1/5/07) to allow to intervene [1015636-1]. Motion filed by CT Dept Pub Util
01/08/2007	MOTION filed (5 copies) (certificate of service dated 1/8/07) to allow to intervene [1015637-1]. Motion filed by TransCan Power Mkt
	* * * * *
01/09/2007	MOTION filed (5 copies) (certificate of service dated 1/9/07) to allow to intervene [1015639-1]. Motion filed by Intl Power Amer Inc
	* * * * *
01/10/2007	MOTION filed (5 copies) (certificate of service dated 1/10/06) to allow to intervene [1015647-1]. Motion filed by Bridgeport Engy, Casco Bay Engy Co
	* * * * *

DATE	PROCEEDINGS
01/10/2007	MOTION filed (5 copies) (certificate of service dated 1/9/07) to allow to intervene [1015652-1]. Motion filed by New England Power
	* * * * *
01/10/2007	CLERK'S ORDER filed [1015655] to consolidate cases 06-1403 and 06-1427 [1015655-1] and directing Petitioner in 06-1427 to file [1015655-2] docketing statement and statement of issues by 2/9/07. [Entry Date: 1/10/07] [06-1403, 06-1427]
01/10/2007	MOTION filed (5 copies) (certificate of service dated 1/10/07) to allow to intervene [1015789-1]. Motion filed by Milford Power Co in 06-1403
	* * * * *
01/10/2007	MOTION filed (5 copies) (certificate of service dated 1/10/07) to allow to intervene [1016178-1]. Motion filed by FPL Engy in 06-1403, Entergy Nuc Genrtn in 06-1403, Entergy Nuc VT in 06-1403, Mirant Engy Trdg in 06-1403, Mirant Kendall in 06-1403, Mirant Canal LLC in 06-1403, Boston Genrtn in 06-1403, Mystic I LLC in 06-1403, Mystic Devel in 06-1403, Fore Riv Devel in 06-1403
	* * * * *
01/11/2007	MOTION filed (5 copies) (certificate of service dated 1/10/07) to allow to intervene [1016190-1]. Motion filed by Richard Blumenthal in 06-1403

DATE	PROCEEDINGS
01/11/2007	MOTION filed (5 copies) (certificate of service dated 1/10/07) to allow to intervene [1016194-1]. Motion filed by Indust Engy Consum in 06-1403 (corporate disclosure information contained within the motion)
01/11/2007	MOTION filed (5 copies) (certificate of service dated 1/11/07) to allow to intervene [1016503-1]. Motion filed by NEPOOL Indust Cust in 06-1403
	* * * * *
01/11/2007	MOTION filed (5 copies) (certificate of service dated 1/10/07) to allow to intervene [1016505-1]. Motion filed by NRG Power Mkt Inc in 06-1403, CT Jet Power LLC in 06-1403, Devon Power LLC in 06-1403, Norwalk Power LLC in 06-1403, Middletown Power in 06-1403, Montville Power in 06-1403, Somerset Power LLC in 06-1403
	* * * * *
01/11/2007	MOTION filed (5 copies) (certificate of service dated 1/11/07) to allow to intervene [1016512-1]. Motion filed by CT Muni Elec Engy in 06-1403
01/11/2007	MOTION filed (5 copies) (certificate of service dated 1/11/07) to allow to intervene [1016515-1]. Motion filed by ISO New Engl Inc in 06-1403
	* * * * *

DATE	PROCEEDINGS
01/11/2007	MOTION filed (5 copies) (certificate of service dated 1/11/07) to allow to intervene [1016525-1]. Motion filed by Lake Rd Gentrn Co in 06-1403
	* * * * *
01/12/2007	MOTION filed (5 copies) (certificate of service dated 1/12/07) to allow to intervene [1016537-1]. Motion filed by NSTAR Elec Gas Corp in 06-1403
	* * * * *
01/12/2007	INITIAL SUBMISSIONS filed by Petitioner ME Pub Util Cmsn in 06-1403 [1016647-1]: docketing statement; certificate of counsel; statement of issues; deferred appendix notice (Deferred Appendix needed = y).
	* * * * *
01/17/1007	MOTION filed (5 copies) (certificate of mail service dated 1/17/07) to allow to intervene [1017309-1]. Motion filed by Berkshire Power Co in 06-1403
	* * * * *
01/23/2007	MOTION filed (5 copies) (certificate of mail service dated 1/23/07) to allow to intervene [1018198-1]. Motion filed by MASSPOWER in 06-1403
	* * * * *

DATE	PROCEEDINGS
01/24/2007	MOTION filed (5 copies) (certificate of service dated 1/24/07) to allow to intervene [1018434-1]. Motion filed by Dominion Resrc Inc in 06-1403, Dominion Engy Mkt in 06-1403, Dominion Nuc CT in 06-1403
	* * * * *
01/26/2007	MOTION filed (5 copies) (certificate of service dated 1/26/07) to allow to intervene [1020171-1]. Motion filed by Ctrl VT Pub Svc Corp in 06-1403
	* * * * *
01/29/2007	INITIAL SUBMISSIONS filed by Respondent FERC in 06-1403 and 06-1427 [1020084-1]: certified index to the record. [06-1403, 06-1427]
01/29/2007	MOTION filed (5 copies) (certificate of service dated 1/26/07) to allow to intervene [1020207-1]. Motion filed by PSEG Power in 06-1403, PSEG Engy Resrc Trd in 06-1403
	* * * * *
02/07/2007	CLERK'S ORDER filed [1021638] granting non-party motion to intervene filed by PSEG Power, PSEG Engy Resrc Trd [1020207-1] in 06-1403 granting non-party motion to intervene filed by Ctrl VT Pub Svc Corp [1020171-1] in 06-1403 granting non-party motion to intervene filed by Dominion Resrc Inc, Dominion Engy Mkt, Dominion Nuc CT [1018434-1] in 06-1403 granting non-party motion to intervene filed by MASSPOWER [1018198-1] in 06-1403 granting non-party motion to intervene filed by Berk-

DATE	PROCEEDINGS
	shire Power Co [1017309-1] in 06-1403 granting non-party motion to intervene filed by NSTAR Elec Gas Corp [1016537-1] in 06-1403 granting non-party motion to intervene filed by Richard Blumenthal [1016190-1] in 06-1403 granting non-party motion to intervene filed by Indust Engy Consum [1016194-1] in 06-1403 granting non-party motion to intervene filed by NEPOOL Indust Cust [1016503-1] in 06-1403 granting non-party motion to intervene filed by NRG Power Mkt Inc, CT Jet Power LLC, Devon Power LLC, Norwalk Power LLC, Middletown Power, Montville Power, Somerset Power LLC [1016505-1] in 06-1403 granting non-party motion to intervene filed by MA Muni Whsle Elec [1016508-1] in 06-1403 granting non-party motion to intervene filed by CT Muni Elec Engy [1016512-1] in 06-1403 granting non-party motion to intervene filed by ISO New Engl Inc [1016515-1] in 06-1403 granting non-party motion to intervene filed by Lake Rd Gentrn Co [1016525-1] in 06-1403 granting non-party motion to intervene filed by Bridgeport Engy, Casco Bay Engy Co [1015647-1] in 06-1403 granting non-party motion to intervene filed by New England Power [1015652-1] in 06-1403 granting non-party motion to intervene filed by Milford Power Co [1015789-1] in 06-1403 granting non-party motion to intervene filed by FPL Engy, Entergy Nuc Genrtn, Entergy Nuc VT, Mirant Engy Trdg, Mirant Kendall, Mirant Canal LLC, Boston Genrtn, Mystic I LLC, Mystic Devel, Fore Riv Devel [1016178-1] in 06-1403 granting non-party

DATE	PROCEEDINGS
	motion to intervene filed by Intl Power Amer Inc [1015639-1] in 06-1403 granting non-party motion to intervene filed by TransCan Power Mkt [1015637-1] in 06-1403. [Entry Date: 2/7/07] [06-1403, 06-1427]
02/09/2007	CLERK'S ORDER filed [1022209] granting non-party motion to intervene filed by CT Dept Pub Util [1015636-1]. [Entry Date: 2/9/07]
02/09/2007	INITIAL SUBMISSIONS filed by Petitioner Richard Blumenthal in 06-1427 [1023221-1]: docketing statement and statement of issues. [filed in No. 06-1427]
	* * * * *
02/20/2007	NOTICE OF INTENT filed by Intervenor NSTAR Elec Gas Corp in 06-1403 advising their support of petitioners Blumenthal Aty Gen for CT and Coakley, Aty Gen for MA. Certificate of service date 2/20/07
02/23/2007	MOTION filed (5 copies) (certificate of service dated 2/23/07) to allow amicus curiae [1025472-1]. Motion filed by PJM Interconnection [06-1403, 06-1427]
	* * * * *
03/05/2007	CLERK'S ORDER filed [1026384] granting non-party motion to allow amicus filed by PJM Interconnection [1025472-1] in 06-1403, 06-1427. [Entry Date: 3/5/07] [06-1403, 06-1427]
	* * * * *

DATE	PROCEEDINGS
06/08/2007	PETITION FOR REVIEW CASE docketed. Petition for Review filed by Petitioner ME Pub Util Cmsn. [1046073-1] [filed in No. 07-1193]
06/08/2007	MOTION filed (5 copies) by Petitioner ME Pub Util Cmsn in 07-1193 (certificate of mail service dated 6/8/07) to consolidate cases [1046080-1] 06-1403 and 07-1193. [06-1403, 07-1193]
06/14/2007	RESPONSE lodged [1047167-1] (5 copies) by Movant-Intervenor New England Power in 07-1193 (certificate of mail service dated 6/13/07) to a motion [to] consolidate case [1046080-1] in 07-1193, to a motion [to] consolidate case [1046080-1] in 06-1403. [07-1193, 06-1403]
06/21/2007	PER CURIAM ORDER filed [1048550] establishing the initial briefing schedule and format [1048550-1]: Petitioners' briefs (14,000 wds between the two briefs) due on 8/20/07; Intervenors supprtng petitioners' joint brief, 8,750 wds, due 9/4/07; Respondent's brief, 14,000 wds, due on 10/19/07; Intervenors briefs in support of respondent (brief of ISO-NE, 2,500 wds; briefs of CT-DPUC and the remaining intervenors in support of respondent, 8,750 wds between the two briefs) due 11/6/07; Amicus Curiae PJM Interconnection [()7,000 wds) due on 11/6/07; Petitioners' reply briefs (not to exceed a total of 7,000 wds between the two briefs) due on 11/26/07; Intervenor supprt Petitioners reply brief, 4,375 wds, due 11/26/07; Deferred appendix due on 12/17/07; Final briefs 12/31/07. Parties will be notified

DATE	PROCEEDINGS
	by separate order of oral argument date and composition of merits panel. Before Judges Sentelle and Tatel. [Entry Date: 6/21/07] [06-1403, 06-1427]
06/21/2007	CLERK'S ORDER filed [1048553] granting motion [to] consolidate cases filed by ME Pub Util Cmsn [1046080-1] (07-1193) in 06-1403, 07-1193. Briefing format and schedule established by court's 6/21/07 order remains in effect. [Entry Date: 6/21/07] [06-1403, 06-1427, 07-1193]
07/18/2007	INITIAL SUBMISSIONS filed by Respondent FERC [1055145-1]: CORRECTED certified index to the record. [06-1403, 06-1427, 07-1193]
07/18/2007	SUPPLEMENT to [1055149-1] Corrected certified index to the record [1055145-1] filed by Respondent FERC. [06-1403, 06-1427, 07-1193]
08/20/2007	BRIEF filed by Petitioners ME Pub Util Cmsn in 06-1403 and 07-1193 and Richard Blumenthal and Martha Coakley in 06-1427 [1063135-1]. Copies: 7. Certificate of service date 8/20/07. [06-1403, 06-1427, 07-1193]
09/05/2007	BRIEF filed by Intervenors Indust Engy Consum, NSTAR Elec Gas Corp and NEPOOL Indust Cust in 06-1403 [1070626-1]. Copies: 15. Certificate of service date 9/4/07.

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DATE	PROCEEDINGS
10/19/2007	BRIEF filed by Respondent FERC in 06-1403, 06-1427 and 07-1193 [1079342-1]. Copies: 7. Certificate of service date 10/19/07. [06-1403, 06-1427, 07-1193]
11/06/2007	BRIEF filed by Intervenor FPL Engy, et al., in 06-1403, [1080247-1]. Copies: 7. Certificate of service date 11/6/07.
11/06/2007	BRIEF filed by Intervenor ISO New Engl Inc in 06-1403 [1080269-1]. Copies: 7. Certificate of service date 11/6/07.
11/06/2007	BRIEF lodged by Amicus Curiae for Respondent PJM Interconnection in 06-1403, Movant-Amicus Curiae PJM Interconnection in 06-1427 [1080281-1]. Copies: 15. Certificate of service date 11/6/07. [06-1403, 06-1427] (Replaced by Corrected Brief on 11/21/07)
11/21/2007	CORRECTED BRIEF filed by Amicus Curiae for Respondent PJM Interconnection in 06-1403, Movant-Amicus Curiae PJM Interconnection in 06-1427 [1084244-1]. Copies: 15. Certificate of service date 11/21/07. [06-1403, 06-1427] (Replaces Lodged Brief of 11/6/07)
11/26/2007	REPLY BRIEF filed by Petitioner ME Pub Util Cmsn in 06-1403, Petitioner Richard Blumenthal in 06-1427, Petitioner Martha Coakley in 06-1427, Petitioner ME Pub Util Cmsn in 07-1193 [1084225-1]. Copies: 7. Certificate of service date 11/26/07. [06-1403, 06-1427, 07-1193]

DATE	PROCEEDINGS
11/27/2007	REPLY BRIEF lodged by Intervenor Indust Engy Consum, et al., in 06-1403 [1084179-1]. Copies: 7. Certificate of service date 11/26/07. (Replaced by reply brief lodged on 12/5/07)
	* * * * *
12/05/2007	CORRECTED REPLY BRIEF lodged by Intervenor Indust Engy Consum in 06-1403 [1085797-1]. Copies: 7. Certificate of service date 12/4/07 (Replaces reply brief lodged on 11/27/07)
12/05/2007	MOTION filed (5 copies) by Intervenor Indust Engy Consum in 06-1403 (certificate of service, by mail, dated 12/4/07) for leave to file [1085801-1] a corrected reply brief [1085797-1].
12/17/2007	DEFERRED APPENDIX (3 Volumes) filed by Petitioner ME Pub Util Cmsn in 06-1403, Petitioner ME Pub Util Cmsn in 07-1193 [1087303-1]. Copies: 10. Certificate of service date 12/17/07. [06-1403, 07-1193]
12/20/2007	ERRATA to [1089734-1] appendix [1087303-1] in 06-1403, appendix [1087303-1] in 07-1193 filed by Petitioner ME Pub Util Cmsn in 06-1403, Petitioner ME Pub Util Cmsn in 07-1193. [06-1403, 07-1193]
12/28/2007	CORRECTED BRIEF lodged by Intervenors Indust Engy Consum, NSTAR Elec Gas Corp and NEPOOL Indust Cust in 06-1403 [1089030-1]. Copies: 15. Certificate of service date 12/27/07.

DATE	PROCEEDINGS
12/28/2007	MOTION filed (5 copies) by Intervenors for Petitioner Indust Engy Consum, NEPOOL Indust Cust and NSTAR Elec Gas Corp in 06-1403 (certificate of service by mail dated 12/27/07) for leave to file [1089032-1] a corrected brief [1089030-1].
12/28/2007	FINAL BRIEF filed by Intervenor FPL Engy, et al., in 06-1403, 06-1427 and 07-1193 [1089822-1]. Copies: 15. Certificate of service date 12/28/07. [06-1403, 06-1427, 07-1193]
12/28/2007	BRIEF filed by Intervenor ISO New Engl Inc in 06-1403 [1089843-1]. Copies: 15. Certificate of service date 12/28/07. [06-1403, 06-1427, 07-1193]
12/28/2007	FINAL REPLY BRIEF filed by Intervenor for Petitioner Indust Engy Consum, et al., in 06-1403 [1089853-1]. Copies: 15. Certificate of service date 12/27/07. [06-1403, 06-1427, 07-1193]
12/31/2007	FINAL BRIEF filed by Petitioner ME Pub Util Cmsn in 06-1403, Petitioner Richard Blumenthal in 06-1427, Petitioner Martha Coakley in 06-1427, Petitioner ME Pub Util Cmsn in 07-1193 [1089804-1]. Copies: 15. Certificate of service date 12/31/07. [06-1403, 06-1427, 07-1193]
12/31/2007	FINAL BRIEF filed by Respondent FERC in 06-1403, Respondent FERC in 06-1427, Respondent FERC in 07-1193 [1089812-1]. Copies: 15. Certificate of service date 12/31/07. [06-1403, 06-1427, 07-1193]

DATE	PROCEEDINGS
12/31/2007	FINAL BRIEF filed by Amicus Curiae for Respondent PJM Interconnection in 06-1403, Movant-Amicus Curiae PJM Interconnection in 06-1427 [1089849-1]. Copies: 15. Certificate of service date 12/31/07. [06-1403, 06-1427, 07-1193]
12/31/2007	FINAL REPLY BRIEF filed by Petitioner ME Pub Util Cmsn in 06-1403, Petitioner Richard Blumenthal in 06-1427, Petitioner Martha Coakley in 06-1427, Petitioner ME Pub Util Cmsn in 07-1193 [1089852-1]. Copies: 15. Certificate of service date 12/31/07. [06-1403, 06-1427, 07-1193]
01/09/2008	CLERK'S ORDER filed [1091012] to schedule oral argument [1091012-1] before Judge Initials: JWR MBG LHS on 2/14/08 at 9:30 AM. [Entry Date: 1/9/08] [06-1403, 06-1427, 07-1193]
01/09/2008	CLERK'S ORDER filed [1091146] granting motion of intervenors in support of petitioners to file corrected reply brief and directing Clerk to file the lodged brief. [Entry Date: 1/9/08] [06-1403, 06-1427, 07-1193]
01/09/2008	CLERK'S ORDER filed [1091150] granting motion for leave to file corrected brief of intervenors in support of petitioners and directing Clerk to file the lodged brief. [Entry Date: 1/9/08] [06-1403, 06-1427, 07-1193]
01/09/2008	PER ABOVE ORDERS lodged intervenor's brief and lodged reply brief filed [06-1403, 06-1427, 07-1193]

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DATE	PROCEEDINGS
02/12/2008	LETTER filed by Intervenors Mirant Canal LLC, et al. pursuant to FRAP 28j advising of additional authorities [1098961-1]. Certificate of service date 2/12/08. [06-1427, 06-1403, 07-1193]
02/14/2008	ORAL ARGUMENT HELD before Rogers, Garland, Silberman. [06-1403, 06-1427, 07-1193]
	* * * * *
03/28/2008	PER CURIAM JUDGMENT filed [1108074] The petitions for review are granted in part, denied in part, and remanded for the reasons in the accompanying opinion. Judge Rogers, Garland and Silberman [06-1403, 06-1427, 07-1193]
03/28/2008	OPINION filed [1108079] PER CURIAM OPINION (Pages: 29) [06-1403, 06-1427, 07-1193]
03/28/2008	CLERK'S ORDER filed [1108081] withholding issuance of the mandate. [06-1403, 06-1427, 07-1193]
04/14/2008	MOTION filed [1111044] by FERC in 07-1193 Styled as Expedited Motion for Extension of Time to Petition for Rehearing and to Stay Issuance of Mandate of Respondent Federal Energy Regulatory Commission (Response to Motion served by mail due on 04/28/2008) [Mail and Electronic Mail Service Date: 04/14/2008] Copies: 5 (Motion/Petition); Pages: 5; Disclosure Statement: Not Applicable to this Party; Certificate of Parties: Previously Filed [06-1403, 06-1427, 07-1193] (MOTION TO STAY WITH-

DATE	PROCEEDINGS
	DRAWN PER ORDER ON 5/1/08)—[Edited 05/01/2008 by MCM]
04/18/2008	RESPONSE IN SUPPORT FILED [1112741] by NRG Energy, Inc. and Connecticut Jet Power, LLC, Devon Power, LLC, Entergy Nuclear Generation Company, LLC, Entergy Nuclear Vermont Yankee, LLC, FPL Energy, LLC, Mirant Canal, LLC, Mirant Energy Trading, LLC, Mirant Kendall, LLC, Norwalk Power, LLC and Somerset Power, LLC in 06-1403 to motion to expedite ruling, [1111044-4], motion to extend time, [1111044- 2], motion to stay mandate, [1111044-3] [Service Date: 04/18/2008 US mail] Copies: 5 (Motion/Petition); Pages: 1-10; Disclosure Statement: Previously Filed; Certificate of Parties: Not Applicable to this Filing [06-1403, 06-1427, 07-1193]
04/18/2008	RESPONSE IN OPPOSITION FILED [1112761] by Mr. Richard Blumenthal, Industrial Energy Consumer Group and Maine Public Utilities Commission in 06-1403, Mr. Richard Blumenthal and Martha Coakley in 06-1427, Maine Public Utilities Commission in 07-1193 to motion to expedite ruling, [1111044-4] and motion to stay mandate, [1111044-3] RESPONSE IN OPPOSITION FILED to motion to extend time, [1111044-2], [Service Date: 04/18/2008 US mail] Copies: 5 (Motion/Petition); Pages: 1-10; Disclosure Statement: Previously Filed; Certificate of Parties: Not Applicable to this Filing [06-1403]

DATE	PROCEEDINGS
04/21/2008	REPLY IN SUPPORT FILED [1112093] by FERC in 06-1403, 06-1427, 07-1193 to motion to expedite ruling, [1111044-4], motion to extend time, [1111044-2], motion to stay mandate, [1111044-3] [Service Date: 04/21/2008 US mail] Copies: 5 (Response/Reply); Pages: 1-10; Disclosure Statement: Not Applicable to this Party; Certificate of Parties: Not Applicable to this Filing [06-1403, 06-1427, 07-1193]
05/01/2008	PER CURIAM ORDER filed [1114207] that the motion to stay mandate [1111044-3] be withdrawn. The Clerk is to note the docket accordingly. It is FURTHER ORDERED that the motion to extend time [1111044-2] be granted. Any petition for rehearing and/or rehearing en banc is now due 45 days after the disposition by the United States Supreme Court of Morgan Stanley Capital Group, Inc. v. Public U[ ]tility[ ] District No. 1 of Snohomish County, WA, et al. Nos. 06-1457 and 06-1462 (argued Feb. 19, 2008) Judge Rogers, Garland and Silberman [06-1403, 06-1427, 07-1193]
07/09/2008	TRANSCRIPT [1126618] of oral argument [06-1403, 06-1427, 07-1193]
07/09/2008	MANDATE ISSUED to [06-1403, 06-1427, 07-1193]

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DATE	PROCEEDINGS
08/08/2008	PETITION filed [1132660] by Respondent FERC for rehearing, for rehearing en banc. [Service Date: 08/08/2008] Copies: 20 (En Banc Filing); Pages: 11-15; Disclosure Statement: Not Applicable to this Party; Certificate of Parties: Attached [06-1403, 06-1427, 07-1193]
08/11/2008	CLERK'S ORDER filed [1132459] recalling mandate [06-1403, 06-1427, 07-1193]
08/11/2008	PETITION filed [1132815] by Intervenors Boston Generating, LLC, Connecticut Jet Power, LLC, Devon Power, LLC, Entergy Nuclear Generation Company, LLC, Entergy Nuclear Vermont Yankee, LLC, FPL Energy, LLC, Fore River Development, LLC, Middletown Power, LLC, Mirant Canal, LLC, Mirant Energy Trading, LLC, Mirant Kendall, LLC, Montville Power, LLC, Mystic Development, LLC, NRG Power Marketing, Inc., Norwalk Power, LLC and Somerset Power, LLC for rehearing, for rehearing en banc. [Service Date: 08/11/2008] Copies: 20 (En Banc Filing); Pages: 11-15; Disclosure Statement: Attached; Certificate of Parties: Attached [06-1403]
	* * * * *
08/13/2008	MANDATE RETURNED [1133032]. [06-1403, 06-1427, 07-1193]

DATE	PROCEEDINGS
08/18/2008	Modified Event SUPPLEMENTAL APPENDIX [1134106] lodged [Volumes: 1] [Number of Paper Copies: 10 (Appendix)] [Service Date: 08/15/2008] [06-1403, 06-1427, 07-1193]—[Edited 08/19/2008 by MAM]
08/18/2008	MOTION filed [1134109] by NEPOOL Industrial Customer Coalition and Maine Public Utilities Commission in 06-1403 for leave to file supplemental appendix (Response to Motion served by mail due on 09/02/2008) [Service Date: 08/15/2008] Copies: 5 (Motion/Petition); Pages: 1-10; Disclosure Statement: Previously Filed; Certificate of Parties: Not Applicable to this Filing [06-1403, 06-1427, 07-1193]
08/22/2008	CLERK'S ORDER filed [1134809] directing joint response to petition for rehearing and rehearing en banc [1132815-3]. The joint response may not exceed 15 pages. Response due 09/08/2008. [1132815-2] [1132660-3]; [1132660-2] [06-1403, 06-1427, 07-1193]
09/08/2008	RESPONSE FILED [1137361] by Mr. Richard Blumenthal in 06-1403, 06-1427 to petition for rehearing en banc [1132815-3], petition for rehearing [1132815-2], petition for rehearing en banc [1132660-3], petition for rehearing [1132660-2] [Service Date: 09/08/2008] Copies: 5 (Response/Reply); Pages: 11-15; Disclosure Statement: Attached; Certificate of Parties: Not Applicable to this Filing [06-1403, 06-1427, 07-1193]

DATE	PROCEEDINGS
10/06/2008	PER CURIAM ORDER filed [1142428] granting motion for leave to file a supplemental appendix [1134109-2]; The Clerk is directed to file the lodged appendix [1134106-2] Judge Rogers, Garland and Silberman [06-1403, 06-1427, 07-1193]
10/06/2008	PER ABOVE ORDER lodged supplemental appendix [1134106-2] is filed [06-1403, 06-1427, 07-1193]
10/06/2008	PER CURIAM ORDER, En Banc, filed [1142434] denying petition for rehearing en banc [1132815-3] in 06-1403. Judge Sentelle, Ginsburg, Henderson, Randolph, Rogers, Tatel, Garland, Brown, Griffith, Kavanaugh and Silberman [06-1403, 06-1427, 07-1193] (Circuit Judges Ginsburg and Henderson did not participate in this matter)
10/06/2008	PER CURIAM ORDER filed [1142439] denying petition for rehearing [1132815-2] in 06-1403. Judge Rogers, Garland and Silberman [06-1403, 06-1427, 07-1193]
10/06/2008	PER CURIAM ORDER, En Banc, filed [1142440] denying petition for rehearing en banc [1132660-3] in 06-1403. Judge Sentelle, Ginsburg, Henderson, Randolph, Rogers, Tatel, Garland, Brown, Griffith, Kavanaugh and Silberman [06-1403, 06-1427, 07-1193] (Circuit Judges Ginsburg and Henderson did not participate in this matter)
10/06/2008	PER CURIAM ORDER filed [1142443] denying petition for rehearing [1132660-2] in 06-1403. Judge Rogers, Garland and Silberman [06-1403, 06-1427, 07-1193]

DATE	PROCEEDINGS
10/22/2008	MANDATE ISSUED to FERC [06-1403, 06-1427, 07-1193]
11/24/2008	LETTER filed [1155370] by the Clerk of the Supreme Court of the United States notifying this court of the following activity in the case before it: A petition for writ of certiorari was filed and placed on the docket as 08-674, on 11/21/2008. [06-1403, 06-1427, 07-1193]
04/28/2009	LETTER filed [1178582] by the Clerk of the Supreme Court of the United States notifying this court of the following activity in the case before it: The petition for writ of certiorari was disposed of on 04/27/2009, with Granted. [06-1403, 06-1427, 07-1193]

UNITED STATES OF AMERICA

BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Devon Power LLC, et al.) Docket Nos. ER03-563-000,
) ER03-563-030, and
ER03-563-055

EXPLANATORY STATEMENT OF THE SETTLING PARTIES IN SUPPORT OF SETTLEMENT AGREEMENT AND REQUEST FOR EXPEDITED CONSIDERATION

(March 6, 2006)

Pursuant to Rule 602 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.602 (2005), the Settling Parties (as identified in the Settlement Agreement and Section V of this Explanatory Statement)[1] submit this "Explanatory Statement of the Settling Parties in Support of Settlement Agreement and Request for Expedited Consideration" ("Explanatory Statement" or

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[1] Capitalized terms used but not defined in this Explanatory Statement are intended to have the meanings given to such terms in the Settlement Agreement, the ISO New England Inc. Transmission, Markets and Services Tariff ("ISO Tariff"), the Participants Agreement, or the Second Restated New England Power Pool Agreement (the "Second Restated NEPOOL Agreement") (as such terms may be consolidated on Attachment A to the Settlement Agreement).

"Statement") with accompanying settlement agreement ("Settlement Agreement" or "Agreement") (Attachment 1) for approval by the Federal Energy Regulatory Commission ("Commission"). As set forth more fully in Section 1 and 2 of the Settlement Agreement, the Settling Parties request, pursuant to Rule 212 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.212, that the Commission approve this Settlement Agreement in its entirety without conditions or modifications on or before June 30, 2006.[2] As explained *infra*, expedition is appropriate because implementation of the Settlement Agreement requires substantial effort to finalize detailed market rules and manuals, and an approval on or before that date permits the necessary detail work to be completed in time to support the December 1, 2006 implementation.

This Settlement Agreement is the result of more than 30 days of noticed, formal settlement conferences among more than 175 parties pursuant to notice by and involvement of Administrative Law Judge Lawrence Brenner (the "Settlement Judge"). Those settlement talks were preceded by 24 days of hearings involving 64 parties, thousands of pages of exhibits, roughly 5000 pages of transcript, and a 283-page initial decision issued on June 15, 2005 (the "Initial Decision").[3] Consistent with Commission direction,[4] the Settling Parties have developed an alternative to the Initial Decision's locational installed capacity ("LICAP") mechanism that would replace the LICAP mechanism to achieve the Commission's goals, as

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[2] Settlement Agreement at §§ 1-2.

[3] *Devon Power LLC, et al.*, 111 FERC ¶ 63,063 (2005) ("Initial Decision").

[4] *Devon Power LLC, et al.*, Docket ER03-563-030, oral argument, September 20, 2005. Tr. 252:20-253:10.

stated in the June 2004 Order.[5] In the long term, the capacity market proposed in the Settlement Agreement establishes a "market-type mechanism"[6] to attract new Resources to meet the growing electric energy needs of the New England region, generally using the Forward Capacity Market ("FCM") design recommended by state regulators and consumer representatives. For a transition period before the FCM, the Settlement Agreement provides a level of compensation to suppliers that is lower than the compensation that would have been paid had the LICAP mechanism approved in the Initial Decision been adopted by the Commission. These transition payments will serve as a bridge to the FCM. The market design, in both the short and long term, also provides a price signal for capacity to perform when needed and facilitates participation in the capacity market by intermittent and demand response resources. As shown in Attachments 2, 3, and 4, Witnesses Robert Stoddard, on behalf of Capacity Suppliers and Dominion, Miles Bidwell, on behalf of the Connecticut Department of Public Utility Control ("CT DPUC"), and Peter Cramton, on behalf of the ISO, support the FCM as a workable market design for the New England region.[7]

Based on polling by the Settlement Judge, this Settlement Agreement has the support of public utility regulators from four of the six New England states, and is either supported or not opposed by a broad cross-section of generation owners, transmission owners, load serving en-

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[5] *Devon Power LLC, et al.*, 107 FERC ¶ 61, 240 at P 1 (2004) ("June 2004 Order").

[6] 107 FERC ¶ 61, 240 at P 7.

[7] Execution of the Settlement Agreement does not imply support, endorsement, or subscription to all or any of the Affidavits, which are being submitted only on behalf of the specific parties listed therein.

tities and ISO New England Inc. (the "ISO"). NEPOOL supports this settlement by a 78.46% vote of its Market[ ] Participants.

I. INTRODUCTION

As demonstrated in this Explanatory Statement, the Settlement Agreement strikes a just, reasonable, and fair balance among suppliers, state public utility regulators, consumer advocates, and load, and should be approved. The Settlement Agreement achieves two fundamental objectives shared by all parties to this case. First, the FCM provides a market structure that will encourage needed new generation to be built. Second, the FCM is designed to allow new capacity to set the clearing price, thus providing a market-based measure of the cost of new entry.

Section II of this Explanatory Statement provides a summary of the case, and Section III contains an overview of the Settlement Agreement. In Section IV, the Settling Parties explain their request for expedited consideration of the Settlement Agreement. Section V identifies the Settling Parties. A more detailed explanation of the Settlement Agreement, along with the information required by the Commission to be included with an explanatory statement, is contained in Section VI. Section VII provides additional details concerning the service of this Settlement Agreement and Explanatory Statement on interested parties, and Section VIII provides a concluding statement.

Notwithstanding the very broad support for this Settlement Agreement, the Settling Parties do expect that aspects of the Settlement Agreement will be opposed. The Maine Public Utilities Commission, the Massachusetts Department of Telecommunications and Energy, and the Massachusetts Attorney General have expressed opposition to the proposed settlement. Although the

Connecticut Department of Public Utility Control and the Connecticut Office of Consumer Counsel support the settlement, the Connecticut Attorney General has stated its opposition. In addition, some transmission-owning utilities and load serving entities do not support the settlement. As will be shown below, however, the Commission should approve the Settlement Agreement, notwithstanding these objections.

It is well settled that the Commission "can approve contested settlements as long as it determines that the proposal will establish just and reasonable rates."[8] The Commission's decision to approve a contested portion of a settlement must be supported by substantial evidence or a finding that, as to the contested matter, there is no genuine issue of material fact.[9] This standard is embedded in section 385.602(h) of the Commission's regulations.[10]

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[8] *New Orleans Public Service, Inc. v. FERC*, 659 F.2d 509, 512 (5th Cir. 1981) (citing *Placid Oil Co. v. FPC*, 483 F.2d 880, 893 (5th Cir. 1973), *aff'd. sub nom. Mobil Oil Corp. v. FPC*, 417 U.S. 283, 312-13, 94 S. Ct. 2328, 2347-48, 41 L. Ed. 2d 72 (1974)).

[9] *Exxon Co., U.S.A. v. FERC*, 182 F.3d 30, 37 (D.C. Cir. 1999). On appeal, a reviewing court "will set aside FERC's approval if it was 'arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law.'" *Id.* However, the test is narrow and the court "is not to substitute its judgment for that of the agency." *Id.* (citing *Motor Vehicle Mfrs. Ass'n of the United States, Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43, 77 L. Ed. 2d 443, 103 S. Ct. 2856 (1983)). Where[ ] the analysis to be performed "requires a high level of technical expertise, [the court] must defer to the informed discretion of the responsible federal agencies." *Id.* Nonetheless, the FERC must engage in rational decision making. *Id.* (citing *Motor Vehicle Mfrs. Ass'n of the United States, Inc.*, 463 U.S. 29 at 43 (1983)).

[10] Section 385.602(h)(i) of the regulations provides that

> If the Commission determines that any offer of settlement is contested in whole or in part, by any party, the Commission may decide the merits of the contested settlement issues, if the record

In addressing a contested settlement, at least four approaches are available to the Commission. The Commission may: (1) make a merits decision on each contested issue; (2) approve the settlement as a package if it determines that the overall result of the settlement is just and reasonable; (3) approve the settlement if its benefits to directly affected parties outweigh objections by contesting parties whose interests are too attenuated; or (4) sever contesting parties.[11] In this instance, the settlement may be approved as a complete package because it represents a just and reasonable result.

The Settling Parties urge the Commission to evaluate and approve the Settlement Agreement as a package. This Settlement Agreement reflects a complex compromise among all affected parties. Each Settling Party might well oppose at least some individual components within the Agreement if taken in isolation, but the Settling Parties together have agreed to the package as a whole.[12] Changing any aspect of the Agreement would upset the balance achieved in the Agreement and will undoubtedly provoke calls to change other aspects of the Agreement. Getting the parties to this point has been an extraordinary challenge and there can be no assurance that conditions or changes, no matter how slight they may appear on the surface, could alter that balance. This Settlement Agreement is a complete package that must

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contains substantial evidence upon which to base a reasoned decision or the Commission determines there is no genuine issue of material fact.

[11] *Trailblazer Pipeline Company*, 85 FERC ¶ 61,345 (1998), *order on reh'g*, 87 FERC ¶ 61,110 (1999).

[12] No Settling Party's support for this Settlement Agreement should be construed as support for any individual component of the Settlement Agreement or for anything more than support for the Settlement Agreement as a whole solely in the context of resolving this proceeding.

be considered in its entirety and should be approved in its entirety as just, reasonable, and in the public interest.

While in certain circumstances the Commission is able to sever parties or issues from a contested settlement and approve the settlement among the settling parties as uncontested, the Settling Parties believe that severance is inappropriate in this instance. Ultimately this settlement will create a structure applicable to all generation and load in the region. Contesting parties cannot be severed and permitted to litigate the applicable transition charges or market design elements in specific situations without affecting the rate charged to and received by Settling Parties. Further, many (if not all) Settling Parties agreed to compromise specifically to avoid the uncertainty of prolonged litigation. Issues cannot be severed without upsetting the balance of the Agreement.

II. SUMMARY OF THE CASE

This proceeding began on February 26, 2003, when Devon Power LLC, Middletown Power LLC, Montville Power LLC, Norwalk Power LLC and NRG Power Marketing Inc. (collectively, "NRG") filed, pursuant to Section 205 of the Federal Power Act ("FPA"),[13] four cost-of-service reliability-must-run ("RMR") agreements covering 1,728 MW of generating capacity located within Connecticut and the Southwest Connecticut ("SWCT") Designated Congestion Areas ("DCAs").

In an order issued April 25, 2003[14] (the "April 2003 Order"), the Commission rejected NRG's RMR agreements, and allowed collection of only going-forward maintenance costs through the tracking mechanism approved in a prior order issued March 25, 2003.[15] The Commission

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[13] 16 U.S.C. § 824d (2000).

[14] *Devon Power LLC, et al.*, 103 FERC ¶ 61,082 (2003).

[15] *Devon Power LLC, et al.*, 102 FERC ¶ 61,314 (2003).

directed the ISO to file a "mechanism that implements location or deliverability requirements in the ICAP or resource adequacy market . . . so that capacity within DCAs may be appropriately compensated for reliability."[16]

Pursuant to the Commission's directive in the April 2003 Order, on March 1, 2004, the ISO submitted a LICAP filing (the "March 1 Filing").[17] The ISO's March 1 Filing was protested and commented on by various parties. Two months later, on June 2, 2004, the Commission issued an order (the "June 2004 Order")[18] conditionally accepting the March 1 Filing, established hearing procedures regarding that filing, and identified issues to be addressed at [the] hearing. The Commission directed the Presiding Administrative Law Judge to issue an initial decision on or before June 1, 2005, and deferred implementation of the LICAP proposal until January 1, 2006.

Following the June 2004 Order, the LICAP proposal was addressed in hearings before Administrative Law Judge Bobbie J. McCartney (the "Presiding Judge"). Twenty-four days of hearings were held, beginning on February 23, 2005, and concluding on March 31, 2005. Following voluminous briefs by all interested parties, the Presiding Judge issued the Initial Decision on June 15, 2005.[19]

In the Initial Decision, the Presiding Judge concluded that the ISO's LICAP proposal, as modified throughout the hearings, was just and reasonable and should be ac-

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[16] April 2003 Order at P 37. The Commission further clarified its findings in an order on rehearing in *Devon Power LLC, et al.*, 104 FERC ¶ 61,123 (2003).

[17] Compliance Filing of ISO New England Inc., Docket No. ER03-563-030 (March 1, 2004).

[18] *Devon Power LLC, et al.*, 107 FERC ¶ 61,240 (2004).

[19] *Devon Power LLC, et al.*, 111 FERC ¶ 63,063 (2005).

cepted by the Commission with certain modifications. That Initial Decision has been the subject of numerous briefs on and briefs opposing exceptions and is still pending before the Commission.

Following the issuance of the Initial Decision, the Commission granted a request by numerous parties for oral argument on alternatives to LICAP.[20] In that same order, the Commission again delayed implementation of LICAP, this time holding that it would not be implemented any earlier than October 1, 2006.

Pursuant to direction of the Commission, on September 13, 2005, parties representing load, including the public utility regulatory commissions for all six states, filed the New England Resource Adequacy Model ("NE-RAM")[21] and the New England Locational Resource Adequacy Model ("NELRAM")[22] structures as proposed alternatives to LICAP. Those alternatives proposed a forward resource auction to procure capacity, a descending clock auction held several years in advance of an installed capacity commitment period, penalties for nonperformance, and a phase-in or transition period.[23] All of

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[20] *Devon Power LLC, et al.*, 112 FERC ¶ 61,179 (2005).

[21] Statement in Support of the New England Resource Adequacy Market, *Devon Power LLC*, Docket ER03-563-030 (Sept. 13, 2005).

[22] Four State Commissions' Proposed Alternative to LICAP[,] *Devon Power LLC*, Docket ER03-563-030 (Sept. 13, 2005).

[23] The filing, joined by the Maine Public Utilities Commission, stated at p. 13:

> Because the performance and payment under [a forward procurement approach] will not occur until 2010, the [state commissions for Maine, New Hampshire, Vermont, and Rhode Island] agree that some payments to existing generation resources are appropriate between the first auction and the initial performance period in 2010. . . . The Commission should direct that the issue of transition payments be resolved through a stakeholder settlement process.

these features of the proposed alternatives have been incorporated into the Settlement Agreement.[24]

On October 21, 2005, the Commission granted the request of multiple parties for appointment of the Settlement Judge.[25] This Settlement Agreement is the product of that settlement process.

III. OVERVIEW OF SETTLEMENT AGREEMENT

A. THE FORWARD CAPACITY MARKET

The Settlement Agreement provides for the implementation of an alternative to LICAP—a forward capacity market (the "FCM") establishing competitive auctions for capacity resources to be held three years ahead of their anticipated need. Consistent with proposals advanced before the Commission by state regulators and load, the forward capacity auction ("FCA"), which will be held annually, will be a descending clock auction. A key element of the auction design is the competitive bidding process that will price all capacity from bids made by new capacity. The bidding will start at two times the agreed starting value of CONE of $7.50/kW-month, so the starting value will be $15 per kW-month in the first auction. Recognizing the need for market liquidity and that circumstances will change as suppliers' capacity commitments come due, the FCM provides for an annual reconfiguration auction two years, one year, and just prior to the Commitment Period and twice-yearly seasonal auctions and monthly auctions just prior to, and during[,] each Commitment Period. Due to software and implementation considerations, however, the first initial auction is expected to be held early in 2008 for a Commit-

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[24] Settlement Agreement at § 11, Parts I.A-C and III (Forward Capacity Auction), Part III.F (descending clock auction), Part V.C.2 (availability penalties) and Part VIII (Transition Period).

[25] *Devon Power LLC, et al.*, 113 FERC ¶ 61,075 (2005) at P 9.

ment Period beginning June 1, 2010.[26] The initial auction for the commitment period beginning June 1, 2011 would be held shortly thereafter.

The parties focused on minimizing the risk of auction failure, either because new proposals for capacity resources do not materialize or because bids to meet future needs are adversely impacted by risk analyses for the new market structure or market power. Acknowledging that uncertainties exist with the initial auctions, the FCM contains a mechanism (specified in Section III.G.4.) that is designed to imitate the principles of a price collar often used on trading floors of large financial markets, which establishes a ceiling on the price for existing capacity resources at 1.4 times the cost of new entry ("CONE"), and a floor of 0.6 times CONE until there have been three successful auctions. In the first year, this means that auction prices for existing capacity can range from $4.50 to $10.50. The FCM also contains provisions to ensure that if there is inadequate supply offered or the structure of competition of offers of new supply is insufficient to ensure a competitive result, necessary new resources are brought into the market while limiting the payment to existing suppliers.

With respect to market power concerns, the FCM provides limited opportunities for existing capacity to impact Capacity Clearing Prices. Except within a specified range, all existing capacity that remains listed is effectively a price taker in each FCA and cannot set the clearing prices to be received by other existing capacity resources. Such existing capacity can seek, however, to forego receiving any capacity revenues for a Commitment Period by submitting bids to de-list from the capacity market (a "De-List Bid").[27] If the Capacity Clearing

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[26] Settlement Agreement at § 11, Part I.C.

[27] Settlement Agreement at § 11, Part III.D.5.

Price falls below the level of a De-List bid, the existing capacity submitting that bid will be allowed to de-list all or a portion of a Resource unless the absence of that Resource would produce reliability problems, in which case the Resource will be entitled to just and reasonable compensation but will not set the Capacity Clearing Price. Existing capacity also will be permitted to bid to retire/permanently de-list their capacity. Again, if the Capacity Clearing Price falls below the level of a retirement/permanent de-list bid, the Resource submitting that bid will be permitted to retire/permanently de-list, subject to reliability limitations. The Market Monitoring Unit will have specifically delineated authority to review and reject bids that are concluded to be improper, subject to appropriate Commission involvement. This review is intended to ensure that neither monopoly nor monopsony market power are inappropriately exercised.

The level of capacity payments paid to capacity resources will be directly and immediately tied to the availability of those resources. Availability metrics were a highly contested issue in hearings. The Settlement Agreement reflects a compromise that adopts a definition of "Shortage Event" that is intended to capture hours when capacity resources are determined to be most needed due to conditions on the system. The Settlement Agreement provides for loss of capacity compensation for capacity resources that fail to perform (subject to certain well-defined excuses) during these Shortage Events. On any critical day, a resource can have their compensation reduced up to 10% of annual FCA Payment if it is not available and, in any month, a resource can lose up to two and one-half months of its annual FCA Payment. The availability provisions in the FCM also have a variety of other mechanisms designed to balance, in the specific context of the settlement, the desire for strong economic incentives for capacity resources to be available when

needed without creating unnecessary payment risk to resources.

Additional understandings have been worked out with respect to gas-fired resources, intermittent resources, and demand resources. Because of the expected critical need for gas-fired resources during winter shortage hour events, the Settlement Agreement provides for future changes to the market rules that will accelerate when bids must be received for the Day-Ahead Energy Markets during the winter months and when the ISO will issue financially binding dispatch schedules for the next day. Because of the continued mismatch between the time when gas can be nominated for delivery day ahead and when the ISO is certain of the need for particular gas-fired generation, the Settlement Agreement provides assurance that gas-fired generation procuring transportation and gas to meet its binding Day-Ahead schedule will be entitled to certain reimbursements for gas purchased in reliance on the schedule but not burned as a result of the actual dispatch of the unit.

In addition, due to the continuing desire to accommodate wind and other intermittent resources, rather than subject them to additional reductions in compensation for failure to operate at rated capacity during Shortage Events, the FCM provides for reduced capacity ratings for these units that will reflect their intermittent nature of performance. Over the next 12 months, FCM market rules that are comparable to supply side resources will be developed for demand-side capacity resources.

Similar to the litigated LICAP proposal, the FCM includes a reduction in payments for capacity (except for self-supplied capacity) equal to the "Peak Energy Rents" ("PER") that would be expected to be received from a hypothetical proxy unit during the Commitment Period. This PER deduction will act as both a[ ] disincentive for

suppliers to raise prices in the energy market and a hedge for load against energy price spikes.

B. TRANSITION TO FCM

A transition period is a necessary part of this settlement because the FCM proposed in the settlement will not result in the purchase of capacity until the 2010/11-Power Year. This leaves a gap between now and 2010/11 that must be filled by an interim compensation arrangement. To address this period, the Settlement Agreement provides for a negotiated level of capacity payments for this interim or transition period. Indeed, the proponents of alternatives to LICAP recognized the need for a transition period. Beginning for the month of December 2006, and extending until the Commitment Period for the first FCA, which is expected to occur on June 1, 2010, these payments start at $3.05/kW-month, and increase to $4.10[/]kW-month, paid to all installed capacity. The capacity product is UCAP on a seasonal basis, with a weighted EFORd availability metric.

While there could be disagreement among the Settling Parties as to the actual level of savings to consumers from this Settlement Agreement when compared to LICAP, there is no question that consumers benefit from the settlement. The detailed comparison of the currently projected prices of LICAP and of the settlement transition payment rates are set forth in the Tables 3 and 4 of the attached affidavit of ISO Vice President of Wholesale Markets Strategy David LaPlante (Attachment 6). Along with the other data and record evidence described below, Mr. LaPlante demonstrates that the settlement transition payment rates would be consistently below the projected prices that likely would have been in effect over the same 4-year period had LICAP, which was found to be just and reasonable in the Initial Decision, been implemented. Accordingly, these settlement provi-

sions should be approved as just and reasonable as part of the overall settlement package. This is particularly true in light of the comprehensive nature of the settlement and the multifaceted balance among a variety of competing interests that included the transition payments.

IV. REQUEST FOR EXPEDITED CONSIDERATION

The Settling Parties respectfully request that the Commission approve the Settlement Agreement without modification or condition no later than June 30, 2006. This schedule is extremely important to achieving the agreement to implement transition payments beginning December 1, 2006, and a first FCA in early 2008. Once the Commission has approved the Settlement Agreement, there will remain many details to be worked out in the stakeholder process, which will provide for consultation with state utility regulatory agencies. For that process to be successful, there must be time for a full review and consideration of the details. The Settlement Agreement proposes that such details for transition can be completed by October 1, 2006, with details for FCM finalized and filed by February 15, 2007. Delay in Commission approval of the Settlement Agreement beyond June 30, 2006, materially increases the risk that the necessary details will not be completed in time for implementation on the schedule required by the Settlement Agreement.

For that reason, Section 2 of the Settlement Agreement provides that it terminates on June 30, 2006, in the absence of a Commission order accepting it. That Section further provides that, if the Commission approves the settlement with modifications or conditions, the Settling Parties have only 30 days to attempt to negotiate modified arrangements that are acceptable to all the Settling Parties.

V. THE SETTLING PARTIES

The parties to the Settlement Agreement (each individually a "Settling Party" and collectively the "Settling Parties") as of the date of this Explanatory Statement are as follows:[28]

American National Power, Inc.
[Associated Industries of Massachusetts]
Boston Generating, LLC
Calpine Eastern Corporation
Calpine Energy Services, L.P.
Cape Wind Associates, LLC
Central Vermont Public Service Corporation
Connecticut Department of Public Utility Control
The Connecticut Light and Power Company
Connecticut Municipal Electric Energy Cooperative
Connecticut Office of Consumer Counsel
Conservation Services Group
Consolidated Edison Energy, Inc.
[Coral Power, LLC]
Dominion Energy Marketing, Inc.
Dominion Nuclear Connecticut, Inc.
Dominion Resources, Inc.[ ]
Duke Energy North America, LLC
Energy Management, Inc.
EnerNOC, Inc.
Entergy Nuclear Generation Company

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[28] Mirant New England no longer exists post-bankruptcy. The Mirant companies are:

Mirant Americas Energy Marketing, LP
Mirant Canal, LLC
Mirant Kendall, LLC

Entergy Nuclear Vermont Yankee, LLC
Exelon Generation Company, LLC
[Exelon New England Holdings, LLC]
Fitchburg Gas & Electric Light Company
FPL Energy, LLC
Granite Ridge Energy, LLC
HQ Energy Services (U.S.) Inc.
ISO New England Inc.
Lake Road Generating Company, LP
Long Island Power Authority (LIPA)
MASSPOWER
Milford Power Company, LLC
Mirant Americas Energy Marketing, LP
Mirant Canal, LLC
Mirant Kendall, LLC
Mystic Development, LLC, Mystic I, LLC, and Fore River Development, LLC
National Grid USA (on behalf of itself and its subsidiaries that are intervenors in this proceeding)
NEPOOL Participants Committee
New Hampshire Electric Cooperative, Inc.
New Hampshire Office of Consumer Advocate
New Hampshire Public Utilities Commission
NRG (Devon Power, LLC, Middletown Power LLC, Montville Power LLC, Norwalk Harbor, LLC, and NRG Power Marketing)
[Pinpoint Power]
Public Service Company of New Hampshire
[RI Division of Public Utilities and Carriers]
[RI Public Utilities Commission]
Select Energy
Sempra Trading

[Strategic Energy LLC]
TransCanada Power Marketing Limited
The United Illuminating Company
Vermont Department of Public Service
Vermont Public Power Supply Authority
Vermont Public Service Board
[Wellesley Municipal Light Plant]

Brackets denote signature pages to the Settlement Agreement that have not yet been received.

A number of other parties in the proceeding also have been very engaged and involved in the settlement discussions, but have not submitted executed signature pages by the date of this Statement. For some of those parties, additional processes may be required for approval. Other parties may be continuing to work on resolution of related but independent matters before they are able to support the Settlement Agreement. In addition, while there are others who have indicated opposition to the Settlement Agreement, their representatives have been involved in helping to define key aspects of this agreement.

VI. THE SETTLEMENT AGREEMENT

The Settlement Agreement is included as Attachment 1 to this Explanatory Statement. A more detailed summary of the Settlement Agreement is included below. This section also includes additional information in compliance with the Commission's directives regarding settlement agreements.

A. Compliance with Commission Directives Regarding Information to Be Provided with Settlement Agreements

This Statement, including its attachments and the transmittal letter filed herewith, provides the informa-

tion required by Rule 602 of the Commission's Rules of Practice and Procedure.[29] Pursuant to the October 23, 2003 Notice to the Public entitled "Information to be Provided with Settlement Agreements,"[30] the Settling Parties state as follows:

This Settlement Agreement resolves significant potential issues regarding the LICAP market recommended by the Initial Decision. The Settling Parties have developed an alternative capacity market, the new FCM, that renders moot significant opposition to the recommended LICAP market and, assuming the Settlement is approved, eliminates the need for potential future litigation on the recommended LICAP market. The FCM will be implemented as quickly as possible and, as noted previously, the transition prices are significantly lower than projected prices if the LICAP mechanism adopted in the Initial Decision had been affirmed by the Commission.

The issues being settled have major policy implications: This case presents the fundamental policy issue of how to design a capacity market in order to resolve reliability compensation issues. However, the resolution reflected in this settlement is, by its nature and specific terms, non-precedential. Other than the instant dockets, the Settling Parties are not aware of the results of any other pending cases that will be dictated by Commission action on this Settlement Agreement.[31] The settlement

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[29] 18 C.F.R. § 385.602 (2006).

[30] See "Notice to the Public – Information to be Provided with Settlement Agreements," (issued Oct. 15, 2003); "Errata," (issued Oct. 23, 2003).

[31] The Settlement Agreement does clarify in Part VIII.E. that unless otherwise agreed in a FERC-approved settlement, transition payments will be netted against any RMR payments. Moreover, in Part VIII.F., the Settlement Agreement clarifies that the beginning of transition payments will not trigger automatic termination of RMR agreements that, by their terms, terminate upon the imple-

does not involve an issue of first impression and there are no previous reversals on the issues involved. The Settlement Agreement and the implementing market rules remain subject to the just and reasonable standard established by Sections 205 and 206 of the Federal Power Act, except as specifically provided for in Section 4. of the Settlement Agreement.

In accordance with the December 8, 1999 Notice to the Public entitled "Proposed Settlement Agreements," the Settling Parties are including as Attachment 8 hereto a draft Commission letter order approving the settlement and a diskette containing that letter order in Microsoft Word format.

B. Summary of the Terms of the Settlement Agreement

1. Effectiveness, Termination and Scope of the Agreement

Section 1 of the Settlement Agreement provides that it will become effective either by the Commission approving the agreement in its entirety or, subject to the process described in Section 2, with changes or modifications as agreed by the Settling Parties.

Section 2 sets out provisions for renegotiation if the Commission approves the Settlement Agreement conditionally and termination of the Settlement Agreement if the Commission disapproves the Settlement Agreement or the parties do not accept a Conditional Approval Order. Unless Settling Parties agree to an extension, the Settlement Agreement shall terminate if the Commission does not approve it by June 30, 2006. If the Commission

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mentation or effectiveness of a locational ICAP mechanism but that the start of the first Commitment Period will be considered such implementation or effectiveness for purposes of terminating RMR agreements.

gives only conditional approval (*i.e.*, it modifies any of the Settlement's terms), settlement discussions will be reinstituted for 30 days to permit the Settling Parties to renegotiate and restore the balance of risks and benefits. If the Settling Parties reach agreement, the renegotiated Settlement Agreement will be filed with the Commission. Without a further agreement, the Settlement Agreement will terminate.

The Settlement Agreement resolves all of the issues raised in Docket Nos. ER03-563-030 and ER03-563-055 before the FERC.

2. Market Rules

Section 3 of the Settlement Agreement sets out processes for implementation of the settlement once it is approved by the Commission. First, Section 3.A. details the process for developing the provisions of the ISO Tariff (the "Market Rules") that will be necessary to implement the settlement. The Market Rules will be developed and filed in at least two packages. The first filing will contain rules for implementation of the transition provisions on December 1, 2006, and will be filed by October 1, 2006. The second filing, which must be made by February 15, 2007, will contain the rules for the FCM itself. To the extent addressed in the Settlement Agreement, the parties to the settlement may only challenge the Market Rules on the grounds that they are inconsistent with, or not necessitated by, the Settlement Agreement. Section 3.D. states that the Market Rules will be developed in accordance with NEPOOL's traditional rule review process and will include the opportunity for input from state utility regulators.

Under Section 3.C., a general timeline is laid out for determining a critical input into the FCM—the Installed Capacity Requirement ("ICR"). This process will determine how much capacity will be bought through the auc-

tions. As the Commission is aware, the ISO is currently conducting a stakeholder process in New England (including market participants and state regulators) to review the process for deriving ICR. The goal is to conclude that process during the third quarter of 2006 and, as appropriate, file with the Commission in the fourth quarter of 2006. Based upon the outcome of that filing, the ICR for the first auction will be filed during the third quarter of 2007, with a requested effective date of October 1, 2007, which will enable the first auction to be conducted no later than early 2008. As noted in Section I.C. the first auction will have a truncated Planning Period of slightly over two years, enabling the first Commitment Period to coincide with the June, 2010 through May, 2011 Power Year. Thereafter, auctions will be conducted approximately three and a half years prior to the Commitment Period.

Under Section 4.A., the settling parties waive their Section 206 rights to seek a change in the Settlement Agreement or the Market Rules implementing the agreement for a period of roughly two and one half years (the "Waiver Period"). During this Waiver Period, subject to Section 4.C., the ISO retains its FPA Section 205 rights (subject to appropriate stakeholder processes) but may exercise those rights only upon a showing that the change is needed to prevent a negative effect on system operations or the forward capacity or forward reserves markets. After the Waiver Period, all Settling Parties have their rights provided by law to seek changes.

The Settling Parties agree that two aspects of the settlement require additional special protections against changes. Thus, under Section 4.C., the final prices derived from all auctions and the transition provisions in Section 11, Part VIII cannot be changed unless required by the public interest under the *Mobile Sierra* standard. At least one purpose for adopting the *Mobile-Sierra*

standard for final auction prices is to reduce regulatory uncertainty and thus the risk premium that new entrants may require.

Section 11, Part IX, however, allows parties to challenge key inputs to the auction before the auction is run. Once the auction is run, Section 11, Part II.G.3.b. provides that results from the primary auctions will be filed by the ISO pursuant to Section 205 of the FPA. Parties will have 45 days to file objections to the auction results, and this will be the only means of challenging such results. Section 5 provides that the ISO's internal market monitoring unit will issue a full report analyzing the operations and effectiveness of the FCM 180 days after the second FCA and annually in its Markets Report thereafter.

3. Auction Mechanics

The FCM is a new locational capacity market design that integrates major elements of several proposed forward procurement models—*e.g.*, NERAM and NELRAM (collectively, "RAM Proposals"), and Reliability Options[32]—and the Initial Decision's LICAP. The FCM also shares certain characteristics with the Central Resource Adequacy Market ("CRAM") that was developed as part of the joint discussions of New England, New York and PJM market participants.[33]

Despite the FCM's new name, however, the Commission is acquainted with many elements of the FCM's design. Aspects of FCM were presented in filings and at oral argument before the Commission in September

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[32] Testimony describing Reliability Options is an offer of proof in Docket ER03-563-030. *See* Order Confirming Rulings, Devon Power LLC, ER03-563-030 (Dec. 3, 2004); Hearing Tr. at 1606:16-19.

[33] "Central Resource Adequacy Markets for PJM, NY-ISO and NE-ISO, Final Report" FERC Docket No. ER03-647-004, filed February 26, 2004.

2005. The FCM integrates elements of these market designs and is intended to help assure resource adequacy and reliability for New England at just and reasonable rates, in the context of this settlement package as a whole, as supported by the affidavits of Witnesses Stoddard, Bidwell, and Cramton included as Attachments 2, 3 and 4.

a. Capacity Product Definition and Market Structure

The FCM establishes an auction-based market for locational capacity resources in New England. The product is a megawatt of deliverable capacity with a future supply commitment in a Power Year three years in advance.[34] The three-year period between the auction and the supply commitment period is the Planning Period. The duration of the supply commitment—the Commitment Period—coincides with the June-to-May Power Year and is one year for all existing capacity, but new capacity may choose a Commitment Period of up to five years.[35] The capacity product may be supplied by many types of Capacity Resources, including traditional generating plants, intermittent resources (e.g., wind and hydro),[36] and demand response resources[37] located in New England, as well as imports of capacity resources from outside New England. Partial delisting provisions incorporated into the design permit Capacity Resources to of-

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[34] This is true for all auctions but the first, which has a projected two-year planning period. The first auction is expected to be held by the end of first quarter of 2008 for a commitment period in Power Year 2010/11. All other auctions will have a three-year planning period. For example, capacity for Power Year 2012/13 will be procured in the first quarter of calendar year 2009.

[35] *See* Settlement Agreement, § 11, Part I.B.

[36] *Id.* at Part § 11, II.E.

[37] *Id.*

fer a portion of their capacity in the FCA.[38] As set forth further below, the Settlement Agreement also provides an improved definition of the capacity product by distinguishing the service obligations assumed by the portion of a Resource sold as a capacity ("listed") and the rights retained by the de-listed portion of a resource.[39] Capacity Resources may be designated by a load serving entity to be a self-supplied resource.[40] As discussed below, the FCM includes a locational component that allows for prices to differ in import- or export-constrained zones.

The capacity product is procured in an annual auction administered by the ISO. The amount of capacity that the ISO will procure in the auction is 100 percent of the forecast Installed Capacity Requirement for the appropriate commitment period.[41] A descending clock auction will be used to set the Capacity Clearing Price.[42]

Supplementing the FCA are reconfiguration auctions held prior to and during the Commitment Period.[43] These reconfiguration auctions provide a mechanism for the ISO, suppliers and traders to buy, sell, and exchange capacity obligations and will maintain market liquidity. The FCM includes three types of reconfiguration auctions: (i) three annual auctions (for trading year-long

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[38] *Id.* at § 11, Part II.D.4.

[39] *See generally* Settlement Agreement §11, Part IV.

[40] *Id.* at § 11, Part II.F.

[41] Settlement Agreement, § 11, Part III.C. The ICR is "a measure of the total installed generating capability that the ISO projects is necessary to satisfy its total forecasted load requirements and to maintain sufficient reserve capacity to meet reliability standards." 2006/2007 Power Year Installed Capacity Requirements, *ISO New England Inc.*, Docket No. ER06-656-000 (Feb. 21, 2006) at 6.

[42] *Id.* at § 11, Part III.G.

[43] *Id.* at § 11, § 11, Part III.M.

commitments) before the relevant Commitment Period, (ii) monthly auctions held prior to each commitment month, and (iii) seasonal auctions held prior to June and October of each year to sell a "seasonal strip" product. These reconfiguration auctions preserve any locational element of the initial auction.

b. Participation and Qualification of Capacity Resources

Capacity Resources that participate in the auction will be designated as Existing or New resources.[44] Existing Capacity is a Capacity Resource previously listed as a resource in New England's capacity market. New Capacity has never been listed as a capacity resource. Existing Capacity may also qualify as New Capacity if it undertakes specified types of major investments to upgrade its facilities.[45]

Capacity Resources are required to submit qualification documentation to participate in the auction. Existing Capacity is required to submit documentation, as required by the market rules. In addition, an Existing Capacity Resource that intends to submit a bid to exit the market, permanently or temporarily, may be required to submit information supporting its request to the ISO's Internal Market Monitoring Unit ("Market Monitor").[46] New Capacity must submit documentation demonstrating its control over the proposed project site, a critical path schedule with milestones supporting the feasibility of the project being built, and an interconnection analysis

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[44] *Id.* at § 11, Part II.B, § 11, Part II.D.2.

[45] *Id.* at § 11, Part II.B.2.

[46] The three bid types that enable the Existing Capacity Resource to leave the capacity market are Export Bids, De-list Bids, and Permanent De-list Bids. If any of these bids are greater than a specified price threshold, the bidder is required to submit additional information to the Market Monitor for review.

showing the impact of connecting to the transmission grid.[47] New capacity may also be required to submit documentation supporting their bids to the Market Monitor.

Capacity Resources are also required to provide financial assurances to the ISO. Existing Capacity is generally subject to the requirements of the existing Financial Assurance Policy, Exhibit IA to Section I of the Tariff.[48] New Capacity is required to provide financial assurances as well.[49] When deciding a reasonable level of financial assurances for New Capacity, the Settling Parties weighed the concern that higher credit requirements could raise costs, and a lesser requirement would not sufficiently deter a capacity commitment default. The parties agreed that the Settlement Agreement's financial assurance requirement—an annually increasing provision of credit totaling three months of capacity payments priced at the cost of new entry—is reasonable.[50]

In addition, as described below, the FCM allows resources to self-supply. Load-serving entities ("LSEs") may use owned and contracted resources to self-supply, in whole or in part, the capacity obligations of the loads they serve. Self-supplied resources are required to undertake the same obligations as to qualification and performance as any other Capacity Resources. If designated as self-supplied, the resource will clear the FCA and offset an equal number of megawatts of the projected share of ICR in the Commitment Period for the LSE designating that resource.

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[47] *Id.* at §§ 11, Part II.B.3, II.B.4.

[48] *Id.* at § 11, Parts II.D.2.c., 11, § 11, Part II.G.2.a.

[49] *Id.* at § 11, Part II.G.2.b.

[50] *Id.* at II.G.2.

c. Mechanics of the Descending Clock Auction

In the simplest form of a descending clock auction, the auction administrator announces a starting price—twice the Cost of New Entry ("CONE") under the FCM. Bidders are given specified time to decide how many MW to offer at the current auction price. Following the end of each bidding round, the auctioneer adds up the quantity of resources offered at the stated price. If the number of MW offered is more than the number of MW required, the auctioneer lowers the price for the following round—*i.e.*, the "clock ticks down." Bidders then again decide how much to offer at the lower price. When the total amount of MWs submitted equals the total amount of MWs demanded, the auction closes, and the remaining bidders are winners. Bidders in the clock auction must submit bids in every round, and the number of MW they submit may never be larger than the number of MWs they submitted in a previous round.

The last round of the auction sets the Capacity Clearing Price, which is the price received by all Capacity Resources that are winners and is, in most instances, the price incorporated into the next auction's CONE (which sets the starting price for the next FCA). Consistent with the Commission's objectives, the FCM is designed to price capacity resources accurately to reflect the cost of new entry. In designing the market, a significant challenge essential to market performance is to establish rules assuring that the clearing price is determined competitively. To achieve this outcome, settling parties agreed that price formation by the market will rely primarily on the bids of New Capacity. Existing Capacity's De-list Bids, Export Bids and Permanent De-list Bids, and Imports are eligible to set the Capacity Clearing Price only within specified limits.

CONE is set at $7.50 for the first auction. For all other auctions, CONE is mathematically calculated using the clearing prices of previous auctions.

d. Features of the FCM

Key design elements of the FCM include (1) an auction format to derive competitive prices approximating the cost of new entry, (2) forward procurement of capacity resources, (3) annual commitment periods, (4) opportunities for new entry to participate in the market, (5) procurement of ICR, (6) a locational mechanism to value capacity locationally, when necessary, (7) deductions of PER, (8) market power mitigation rules, and (9) availability-adjusted payments reducing payments for nonperformance and rewarding Resources available during periods of system stress. Each of these elements is discussed below.

First, the FCA is a competitive market for pricing capacity resources. The market-wide FCA price is derived in a central auction administered by the ISO. The FCA price is derived from competing bids of all types of capacity resources: conventional generation, intermittent resources (wind and hydro), and demand response resources.[51]

Several benefits accrue from this market design. First, competing capacity resource suppliers determine the prices. Over time, the compensation received by capacity resources is expected to approximate the cost of new entry, which will appropriately compensate existing generators needed for reliability and attract and retain new entry. Second, capacity resources, without regard to type or technology, receive the same price that clears in the auction. Third, prices that are competitive and paid uniformly across all resources will help New England

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[51] *Id.* at § 11, Part III.G.

achieve the right mix of plant technologies—baseload, intermediate, and peakers. In sum, the competitive pricing will benefit all New England stakeholders by producing efficient prices for capacity resources.

Second, the FCA is forward-looking. The time between the auction and when the capacity resource supplier is obligated to produce is over three years.[52] This three-year Planning Period is intended to provide a planning period for new entry, so that potential new capacity resources can participate in the auction and compete with incumbent resources. If a potential capacity resource wins in the auction, it has more than three years to build the necessary infrastructure needed to fulfill its capacity obligation. If the potential capacity resource is not selected, it can abandon the project or put the project on hold to bid again in the next annual auction. Likewise, if an existing resource is not selected in the FCM, there is a three-year period to allow the orderly transition to alternative, more economic resources. In economic terms, the planning period increases the elasticity of the short-term supply curve (Figure 1) into an elastic long-term supply curve (Figure 2) because suppliers of capacity resources can respond to price movements by changing the amount of capacity they offer in the auction.[53]

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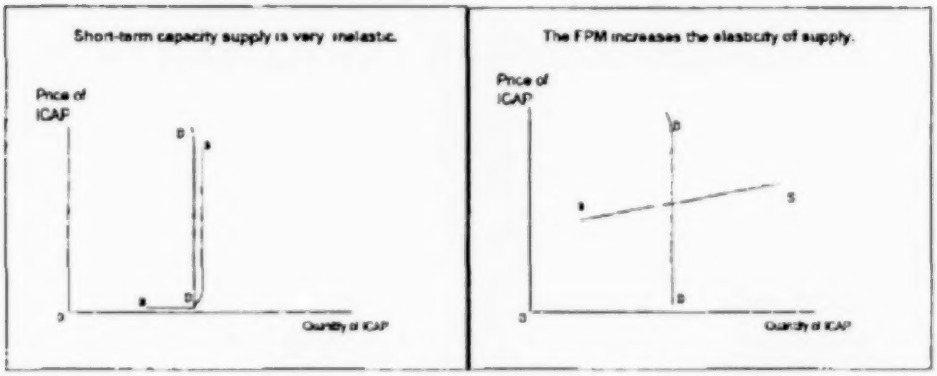
[52] Settlement Agreement, § 11, Part I.B.

[53] *See e.g.*, Motion to Intervene of the New England Conference of Public Utilities Commissioners, Devon Power LLC, Docket No. ER03-563-030 (Mar. 22, 2004), Austin Aff. at P 9 (advocating approach to "design a market where the natural supply curve is more elastic, not fixed [such as] lengthening the supply period to several years so that new and existing generation can compete against one another").

Figure 1 Figure 2



Potential new suppliers of capacity resources benefit from a three-year planning period, as do existing suppliers, in two significant ways. First, decisions whether to build, retire, or repower can be made well in advance of their obligation. Second, the Planning Period provides relief from reliability-based barriers to exit for generating units seeking to retire. If a unit intends to retire from the market, but is unable because the unit is needed for reliability reasons, the three-year period gives developers time to propose and the ISO time to procure the capacity to replace the retiring unit.[54] In addition, a forward-looking capacity market will assist the ISO to prioritize system planning work and to address transmission and resource capacity needs along the horizon.

Third, the capacity product procured in the FCA is committed for a longer period than the current ICAP and proposed LICAP markets, which trade a monthly capacity product. In the FCA, existing suppliers of capacity resources must offer a capacity product with a year-long commitment. The year-long commitment period locking

[54] Settlement Agreement, § 11, Part III.K.

in the capacity price makes near-term revenue streams more predictable.

New capacity suppliers that win the auction are entitled, however, to a one-time option to lock-in capacity prices for up to five years.[55] New suppliers are given this option because it gives investors predictable revenue[ ] streams during the project's early years and should facilitate project financing. Predictable revenue streams are expected to make the project more appealing to financiers and to lower risk premiums charged on the cost of capital. Ultimately, lower risk premiums for new investment will benefit New England ratepayers because new capacity resources may be supplied at lower cost (which means ratepayers will pay less).

Fourth, the FCA facilitates opportunities for new entry in New England's capacity market. Any potential capacity resource is eligible to participate in the auction. New projects proposed must be feasible, so the market rules will require that they fulfill specified criteria to participate in the auction.[56]

Fifth, the ISO will buy the amount of capacity required to maintain the ICR. Each load serving entity (the ultimate purchaser) is required to pay for a share of ICR proportionate to its share of peak load.[57] Because the ISO will only buy ICR, if the system has surplus capacity, not all capacity resources offered will be purchased. Excess capacity resources that are not selected in the auction may retire, mothball, export, or only participate in New England's energy and other markets. The competitive market will send clear signals to any

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[55] *Id.* at § 11, Part I.B.

[56] *Id.* at § 11, Part II.B.3.

[57] *Id.* at § 11, Part III.C.

units that cannot provide lowest-cost capacity to repower or retire, thus opening the grid for New Capacity.

Sixth, the FCM includes a locational component representing New England's import- and export-constrained transmission topologies.[58] Before the auction, capacity zones will be determined by the ISO based on an identification of transmission limits that may bind. If transmission limits (including predicted transmission upgrades that will be on-line by the Commitment Period) are expected to bind, capacity zones are designated, and separate but simultaneous auctions are held for each zone.

This locational component accomplishes the Commission's objectives in three ways. First, the Settlement Agreement's locational component will provide—as the Commission emphasized the need for—"'an incentive . . . in the constrained areas to develop resources or transmission alternatives' to help mitigate potential rate impacts."[59] Second, the locational component will assist to value capacity appropriately in constrained areas. Third, the locational component will configure import-constrained capacity zones to map New England's electrical topology accurately. The need for a locational component will be evaluated by the ISO before each auction, so separate auctions will not be held if the capacity zone is determined to be unnecessary. The dynamic character of zonal designations enables state regulators and load to identify and take actions to eliminate transmission constraints creating capacity zones.

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[58] *Id.* at § 11, Part III.A.

[59] March Order at P 11 (internal citations omitted).

Seventh, except for self-supplied capacity,[60] the FCM includes a deduction from the monthly capacity payment for PER, as in the LICAP model.[61] Under the settlement agreement, however, the PER deduction serves a slightly different purpose because FCA has no demand curve and the PER is not needed to calculate a net CONE value. Under the settlement agreement, the PER deduction primarily acts as a hedge for load against price spikes in the energy market. Because suppliers will be giving back to load energy rents earned by a hypothetical unit in the actual energy market, it also acts as a disincentive for suppliers to exercise market power in the energy market.[62] In the FCM, the PER deduction is determined by calculating the difference between the real time energy price and a strike price derived from the incremental hypothetical cost of a proxy unit. Settlement Agreement, § 11, Part V.B.1. In addition, the PER is converted to a 12-month rolling average and is subtracted from Capacity Resources' monthly capacity payments. *Id.* at § 11, Part V.B.2. The rolling average smoothes month-to-month PER variations to stabilize Capacity Resources' revenue streams from the FCM over a year.

Eighth, the FCM builds in four types of rules to prevent market failures associated with high concentrations of market power, whether held by buyers or sellers. These rules are integrated into the market and are trans-

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[60] The PER adjustment does not apply to Self-Supplied FCA Resources, because the entitlement holders of those Resources are able to credit inframarginal revenues directly against the capacity costs of their Self-Supplied FCA Resources.

[61] Settlement Agreement, § 11, Part V.B.

[62] In this respect it has a similar effect as the PER deduction under the demand curve. *See* ISO-17 (Stoft) at 95:7-17 ("What the energy market gives to an exercise of market power . . . [PER] takes it away").

parent and predictable. Integration, transparency, and predictability allow participants to make their investment and pricing decisions in consideration of these rules.

The first is a set of auction rules that curb incentives to manipulate the market and distort capacity prices. Only specified types of bids can set the auction's clearing price paid to auction winners and incorporated into the successive auctions' CONE.[63] Permanent De-list bids, import bids, export bids, and De-list bids may set the Capacity Clearing Price, but only subject to identified limitations.[64] In addition, specific market rules, such as the Insufficient Competition rule,[65] have been designed to address problems of market failure. The Insufficient Competition rule sets prices for capacity resources if the system (or zone) is short of capacity, the total amount of new capacity bid is small, and any of the new capacity bid is needed to meet ICR (or the local sourcing requirement, if applicable). If the Insufficient Competition rule is triggered, then new capacity resources are paid the Capacity Clearing Price and existing capacity resources are paid the lower of the Capacity Clearing Price or 1.1 CONE.[66]

The second default rule provides for Market Monitor review of bids priced above or below specified price thresholds. *Id.* at § 11, Part III.E. The price thresholds are tied to percentages of CONE. For example, the Market Monitor will review and decide whether to accept into the auction a capacity resource that submits any type of de-list bid (*i.e.*, enabling it to exit the market temporarily or shut down permanently) that is higher

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[63] *Id.* at § 11, Part III.F.

[64] *Id.* at § 11, Part IIIG.H.2.

[65] *Id.* at § 11, Part III.L.2.

[66] *Id.*

than 0.8 CONE. If the Market Monitor determines that the value of the bid is consistent with the resource's net risk-adjusted going-forward and opportunity costs, then the bid is incorporated into the auction.[67] Similarly, a bid from new capacity or imported capacity that is below 0.75 CONE will be reviewed by the Market Monitor, who will determine whether the bid is consistent with the long run average costs of that new capacity resource or the opportunity cost (or another reasonable economic measure) for the import.[68]

The third type of rule, discussed previously, is the three-year planning period that permits new entry to compete with existing capacity resources in the auction and that increases the elasticity of supply by allowing resources to respond to price signals. The fourth rule, also discussed above, assists to mitigate incentives to create price spikes in the energy market. The PER deduction applies similar concepts as the PER deduction proposed in the LICAP model.[69] As in the LICAP market, these revenues are subtracted from capacity payments. The result is that while it may be profitable to raise prices in the energy market, the PER mechanism will remove any profits so gained because the extra revenues earned in the energy market are deducted from capacity payments.

Finally, the FCM contains a mechanism that adjusts capacity payments made to Capacity Resources depending on whether they are available during designated periods of system stress (a "Shortage Event").[70] The purpose of the availability mechanism is, in the specific context of settling this case, to create a strong economic incentive

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[67] *Id.* at § 11, Part III.D.2.

[68] *Id.* at § 11, Part H.1.

[69] *Id.* at § 11, Part V.B.

[70] *Id.* at § 11, Part V.C.

for Capacity Resources to be available when their capacity is most valuable to load—during times of system stress.[71] The FCM rewards responsive and highly available Capacity Resources and reduces capacity compensation to resources that are not available when called by the ISO. Capacity resources that perform poorly for an extended period are expelled from the market until their availability improves.[72]

4. Finality

Several inputs into the auctions will require determinations by the ISO or its Market monitoring unit. These include: (1) determinations of zones (Part III.A.); (2) propriety of specified bids (Part III.D.); and (3) qualification of resources to participate in the auctions (Part II). In order to ensure that the auctions can be conducted with certainty, these inputs must be filed by the ISO as an informational filing no later than 90 days prior to the auction. Parties will have 15 days to file objections. Unless the Commission orders otherwise within 75 days, such determinations will be used in the auction and the results therefrom will be final and subject to the *Mobile Sierra* standard under Section 4.C.

5. Transition Provisions

Because the FCM construct cannot commence until development of market rules and related software, the initial FCA auction is not expected to be held until early in 2008 for a commitment period beginning June 1, 2010. Although the Commission previously anticipated implementation of this new mechanism by "no later than June

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[71] *Id.* at § 11, Part V.C.4 (defining availability).

[72] *Id.* at § 11, Part V.C.7.

1, 2004,"[73] in the absence of transition payment provisions, June 1, 2010, would be the first period for which suppliers would receive payments pursuant to the FCA auction mechanism. Due to the LICAP litigation, no new compensation mechanism has been implemented and, to date, little new generation has been constructed in New England.

Evidence in the record in this proceeding, supplemented by the attached affidavit of ISO Vice President of Markets Development David LaPlante, clearly shows that the transition payments are just and reasonable from the perspective of ratepayers as they are less than the prices that likely would have resulted from LICAP, which was found just and reasonable by Judge McCartney. The transition payments form a bridge to the implementation of the FCM and should help ensure reliable system operation during that time.

In his January 28, 2005 testimony in this proceeding, James Daly, on behalf of the Attorney General of Massachusetts, NSTAR and other parties, projected the following LICAP clearing prices for the 2007-2010 period:[74]

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[73] *Devon Power LLC, et al.*, 103 FERC ¶ 61,082 (2003) at P 33, *quoted in Devon Power LLC, et al.*, 107 FERC ¶ 61,240 (2004) at P 37.

[74] *See* Supplemental Answering Testimony of James G. Daly (Exh. No. Mass AG-17) Table 4 at p. 15. Suppliers do not agree with Mr. Daly's price estimates, which the Initial Decision rejects (111 FERC ¶ 63,063 at P 282), but the estimates nevertheless may be used to illustrate the very large savings that the settlement offers as compared to at least some parties' projected LICAP prices. For example, in spreadsheets provided with that testimony, it appears that Mr. Daly's prices are gross prices and do not reflect a PER deduction. However, even if the $.48 per KW-month PER deduction (which he escalates at 20% per year) that he describes (Exh. No. Mass AG-17, 13:8-11) is subtracted from the prices set forth on Table 1, the proposed settlement transition payment rates are still below his LICAP price projections.

Table 1
Daly's Clearing Price in $/kW-month

	SWCT	ROCT	NEMA	ROP	Maine
2007	$5.31	$5.32	$5.32	$5.32	$5.30
2008	$6.96	$6.96	$6.96	$6.96	$6.96
2009	$8.34	$8.35	$8.33	$8.34	$8.34
2010	$12.29	$12.29	$12.29	$12.29	$12.29

In Mr. LaPlante's Prepared Rebuttal Testimony in this proceeding,[75] he provided the following projected base case and no investment case LICAP clearing prices on a kW/month basis:

Table 2
2006/07-2010-2011 5-Year Average Zonal Prices

	Base Case	No Investment Case
Southwest Connecticut	$6.15	$8.61
Rest of Connecticut	$5.71	$6.54
NEMA/Boston	$4.25	$5.80
Rest of Pool	$3.96	$5.13
Maine	$3.96	$5.13

For these projections, Mr. LaPlante assumed the then current levels of Installed Capacity Requirements, Local Sourcing Requirements, and existing Installed Capacity.[76] For the base case, Mr. LaPlante assumed the level of investment in new generation described in Mr. Karl's

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[75] Prepared Rebuttal Testimony of David LaPlante, Exhibit No. ISO-23, Tables 3 and 4 at 60-61.

[76] These prices do not reflect a PER deduction.

testimony.[77] These low estimates of LICAP clearing prices are now out of date because of significant changes, especially increases in the projections of Installed Capacity Requirements to meet the reliability standard.

Along with his March 16, 2005 supplemental testimony, Mr. Daly provided the following revised clearing prices for the 2007-2010 period.[78] Mr. Daly based the revised projections, in part, on increased Installed Capacity Requirements levels for the 2005/2006 power year that at the time of his March 16 testimony, had recently been approved by the NEPOOL Participants Committee.[79]

Table 3
Daly'[s] Clearing Price in $/kW-month

	SWCT	ROCT	NEMA	ROP	Maine
2007	$7.63	$7.63	$7.63	$7.63	$7.63
2008	$10.21	$10.21	$10.21	$10.21	$10.21
2009	$14.28	$14.25	$14.26	$14.26	$14.26
2010	$16.14	$16.16	$16.16	$16.15	$16.16

In the attached affidavit, Mr. LaPlante,[80] provides the following current projection of LICAP prices based upon the LICAP demand curve adopted in the Initial Decision, and updated data concerning, among other things, In-

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[77] *See* Prepared Rebuttal Testimony of Mark Karl, Exh. ISO-39, 67:8-68:2.

[78] *See* workpaper for Exh. Mass AG-23.

[79] *See* Supplemental Answering Testimony of James G. Daly (Exh. No. Mass AG-23) at 2:8-9:2. Again, Suppliers do not agree with Mr. Daly's price estimates and the Initial Decision rejected them. 111 FERC at P 282.

[80] LaPlante Affidavit at P 11, included as Attachment 5 to this Statement.

stalled Capacity Requirements, Local Sourcing Requirements, and existing installed capacity.[81]

Table 4
LICAP Clearing Price Less PER
($kW-Month)

Zone	2006/07	2007/08	2008/09	2009/10
Connecticut	$4.13	$5.14	$6.39	$11.15
NEMA/Boston	$4.13	$5.14	$6.39	$7.84
Rest of Pool	$4.13	$5.14	$6.39	$7.84
Maine	$4.13	$5.14	$6.39	$7.84

Under the settlement, all listed ICAP Resources shall receive fixed payments, based on the following payment rates and the resources' seasonal UCAP ratings:

Table 5 – Settlement Interim Payment Rates

December 1, 2006 to May 31, 2007	$3.05/kW-month
June 1, 2007 to May 31, 2008	$3.05/kW-month
June 1, 2008 to May 31, 2009	$3.75/kW-month
June 1, 2009 to May 31, 2010	$4.10/kW-month

These numbers show that as the projections have become more recent and reflect more current data, the LICAP price estimates have increased such that the prices calculated pursuant to the LICAP demand curve adopted in the Initial Decision are higher than the proposed settlement transition payments for every zone for every year of the transition period. Although there is no consensus among the Settling Parties as to the precise level of savings to consumers from this Settlement Agreement

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[81] *Id.* at PP 7-10. These are the ISO's numbers and not consensus numbers for the Settling Parties.

when compared to LICAP, there is no question that the transition prices are lower than the prices under LICAP as approved by Judge McCartney.

In the context of the complex and interrelated provisions of the Settlement Agreement, it is appropriate for the transition payments to be the same for all zones in New England. Some have argued that ratepayers in import constrained zones should pay more for capacity than those in capacity surplus zones and that customers in export constrained zones should pay less than those in zones with surplus. This is of course true if the facts demonstrate that zones are actually constrained. However, the price projections described by Mr. LaPlante show nearly flat prices across zones and therefore support interim payments that do not vary on a $/kW-month basis by zone. Nonetheless, as RSP 2005 makes clear, the region's import constrained zones, particularly Connecticut and Boston, have a stronger need for additional capacity than is the case in other regions. However, ratepayers in the constrained zones of Connecticut and NEMA/Boston are already paying substantially more than ratepayers in unconstrained zones such as Maine because of the RMR contracts that are currently required in those constrained regions. The transition period payments agreed to by the parties were negotiated at arms length.

The settlement transition mechanism also includes an availability metric. The Initial Decision recommended that EFORd continue to be used as the availability metric in New England, as requested by Suppliers. That recommendation was vigorously challenged by both the ISO and Load, who sought to measure availability only at times when the region was short of operating reserves or energy. *See, e.g.*, Initial Decision at PP 439-460. The Settlement Agreement reflects a compromise between these two proposals, adopting for the transition period a

modified EFORd that most heavily weights availability during times of greatest need.

As noted above, the Commission's obligation is to determine based on the record whether the Settlement Agreement as a package should be approved. There may be many different calculations of the level of savings to consumers from this settlement when compared to LICAP. The transition payments under the Settlement are clearly lower, however, than the cost of LICAP, as shown here and in Mr. LaPlante's affidavit.

6. Agreement Regarding Rights and Obligations

Part IV of the Settlement Agreement sets forth the rights and obligations of Listed, De-listed and Self-Supplied capacity under the FCM.

a. Listed Capacity

Listed Capacity is any resource participating, or "listed," in the capacity market. Not all of a resource must be listed, and only the listed portion of a resource has the rights and obligations of Listed Capacity.

The key obligation imposed on Listed Capacity is that it must offer into both the Day-Ahead and Real-Time Energy Markets whenever available.[82] In addition, Day-Ahead offers must have a start time plus minimum run time plus minimum down time less than or equal to 72 hours, or, failing that because of "physical design limits," must bid in Day-Ahead at zero, or self-schedule.[83]

Another key obligation imposed on Listed Capacity is that, consistent with good utility practice, the resource's Day Ahead and Real Time offers must reflect the then-known unit-specific operating characteristics of the re-

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[82] Settlement Agreement, § 11, Part IV.A.1.

[83] *Id.* at § 11, Part IV.A.2.

source.[84] Intentionally failing to do so exposes Listed Capacity to significant penalties under the Settlement Agreement. For a first violation, the ISO issues a warning. A second violation incurs a fine of up to the daily FCA payment, capped at $150,000; a third violation incurs a fine of up to two times the daily FCA payment, capped at $300,000; a fourth violation incurs a fine of up to four times the daily FCA payment, capped at $600,000; any further violation permits all remedies under the Federal Power Act, without limitation.[85] Violations may be cumulative (*i.e.*, warning, second, third, and fourth violations) if they occur within a 90-day window, are similar to the original violation and are by the same or a similar unit.[86] If multiple similar units that have their bids submitted by the same entity and all commit the same violation, it will be treated as a single violation.[87] Listed Capacity has specific due process rights with respect to all such warnings and penalties, including timely notice from the ISO within 10 days of the observed behavior, an opportunity to confer, and petition rights at the FERC Office of Market Oversight and Investigations.[88]

Another obligation of Listed Capacity is that it may not go on economic outages.[89] Special bid rules apply, however, in circumstances when "extraordinary fuel prices" prevent a resource from recovering its full operational cost in its bid.[90]

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[84] *Id.* at § 11, Part IV.A.3.

[85] *Id.* at § 11, Part IV.A.4.

[86] *Id.* at § 11, Part IV.A.4.b.

[87] *Id.* at § 11, Part IV.A.4.c.

[88] *Id.* at § 11, Part IV.A.4.d.

[89] *Id.* at § 11, Part IV.A.5.

[90] *Id.*

Finally, Listed Capacity has the right under specified circumstances to transfer its capacity market obligations to another resource.[91] After the transfer, such capacity is treated as De-listed Capacity.

b. De-listed Capacity

The key distinction between Listed Capacity and De-listed Capacity is the latter has no obligation to bid into the Day-Ahead and Real-Time Energy Markets and does not have to honor the ISO's requests to reschedule maintenance.[92] This applies to the portion of a Capacity Resource that (1) does not clear in a FCA, (2) has an accepted Permanent De-list Bid, (3) has an accepted De-list Bid, (4) has an accepted Export Capacity bid and has been de-listed, or (5) has transferred its capacity obligation and is not otherwise committed to provide capacity pursuant to a bilateral contract or reconfiguration auction.[93]

De-listed Capacity may, however, offer into the Day-Ahead Energy Market and, if accepted, would have the same obligations as other resources in the Day-Ahead Market.[94] Further, if bid into the Day-Ahead Market, De-listed Capacity is not subject to the restrictions placed on bidding of unit characteristics for Listed Capacity. De-listed Capacity not offered or accepted in the Day-Ahead Market may only participate in the Real-Time Energy Market by self-scheduling. The ISO may request to commit such resources, but they are not obligated to come on line, and are not subject to any per-

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[91] *Id.* at § 11, Part IV.A.6.

[92] *Id.* at § 11, Part IV.B.2.

[93] *Id.*

[94] *Id.*, § 11, Part IV.B.3.

formance or availability penalties if they do come on line.[95]

Further, since their capacity has not been relied upon to meet the ICR, De-listed Resources are not required to reschedule their maintenance at the ISO's request and De-Listed Capacity may export its capacity. Capacity exports can be transacted either through an accepted Export Bid in the FCM or—subsequent to the FCM—through a bilateral export transaction from De-Listed Capacity.

c. Self-Supplied FCA Resource

Finally, Part IV of the Settlement Agreement establishes that self-supplied resources will have the same rights and obligations as other Capacity Resources accepted in the FCA.[96] The FCM will allow LSEs to use owned or contracted resources to self-supply all or part of their capacity obligations. Resources so designated (a "Self-Supplied Resource") are subject to the same performance obligations and qualification requirements as other Resources participating [in] the FCM and the FCA. The total quantity of designated Self-Supplied Resources may not exceed the projected share of the ICR for the LSE designating that Resource pursuant to Market Rules. To be considered a Self-Supplied Resource, that Resource must be offered into the FCA. In order to qualify as a Self-Supplied Resource for purposes of fulfilling a Local Sourcing Requirement applicable to a load in an import-constrained region, the Self-Supplied Resource must be located in the same Capacity Zone as the associated load, unless the self-supplied resource is a Pool-Planned Unit with a special allocation of CTRs up

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[95] *Id.* at § 11, Part IV.B.4.

[96] *Id.* at § 11, Part IV.C.

to the number of allocated Capacity Transfer Rights ("CTRs").[97]

Together, these provisions in Part IV establish rights and obligations of resources in or out of the FCM so that resources will know how to act. They should be accepted as part of the settlement package.

7. Agreements Regarding Gas Availability

Part VII of the Settlement Agreement addresses a specific problem in coordinating the schedules of the gas and electricity markets in winter months. Under current electric scheduling time frames, gas-fired resources may not have timely information to purchase gas in cold weather periods. They may be unsure of whether and to what extent they will be dispatched the following day. The choice is either to (1) purchase gas and speculatively bear the risk of lost opportunity costs in the event the associated generation is not dispatched and the gas resale market price is significantly lower, or (2) reduce the quantity of gas purchased in advance of the generation schedule. This introduces significant uncertainty for both the gas-fired generator and for the ISO in predicting the availability of gas resources.

Part VII thus provides that—starting in the first FCM and each December, January and February thereafter—the posting of Day-Ahead Market results and the initial Resource Adequacy Assessment will be rolled back to earlier time periods, by a "target completion time" of 10:30 a.m. of the day prior to the electric Operating Day.[98] Other specific scheduling clarifications and adjustments further accommodate gas pipeline nomination deadlines.

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[97] Although the ISO will continue to model any such Pool-Planned Units in their actual location, the combination of the physical asset and the CTRs will offset the financial obligation of the self-supplier.

[98] Settlement Agreement, § 11, Part VII.A.

On days when the ISO forecasts a Cold Weather Warning or Cold Weather Event for the next Operating Day, Part VII also provides that the ISO shall procure an additional 1000 MW of Supplemental Reserves for peak load periods of the day exclusively for gas-fired resources.[99] Gas resources will be compensated for the gas reserved, purchased, and nominated for all such Supplemental Reserves, as set forth by formula.[100]

Finally, on all such days when the ISO forecasts a Cold Weather Warning or Cold Weather Event sufficiently in advance of pipeline gas nominating deadlines, all gas-fired resources are required to confirm to the ISO that they will nominate sufficient fuel to be able to deliver energy and Supplemental Reserves scheduled for the Operating Day.[101]

VII. SERVICE OF THIS PLEADING

This Explanatory Statement, the Settlement Agreement and all attachments have been served on all persons required to be served under Commission rule or order or under law. Pursuant to the agreement of all Settling Parties, this Explanatory Statement, the Settlement Agreement and all attachments have been served on all participants to this proceeding by electronic mail pursuant to the listserv established in this proceeding. The foregoing has also been served on the NEPOOL Participants Committee members by electronic mail, pursuant to section 17.11(e) of the NEPOOL Participants Agreement.

VIII. CONCLUSION

The Commission should approve the Settlement Agreement in its entirety without condition or change.

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[99] *Id.* at § 11, Part VII.B.

[100] *Id.*

[101] *Id.* at § 11, Part VII.C.

The Settlement Agreement resolves issues that have caused intense controversy in the region for years. The long term market design accepts a forward procurement model for capacity that has been advocated by state regulators in all six New England states, and has now been accepted in settlement by virtually all of the generating resources in the region. It is designed to provide economic incentives for Resources to be available when most needed, and it supports participation by all types of Resources, including demand response and intermittent resources. During the transition, FCM is demonstrably less expensive to consumers than LICAP, which the Presiding Judge adopted in the Initial Decision.

At this juncture, it is clear that no settlement is possible that will satisfy all interests. The settlement presented here is widely supported or not opposed by a supermajority of interests in the region. It achieves that support by carefully balancing many conflicting and competing interests. The voluminous record in this proceeding, as well as the supporting affidavits provided on behalf of certain parties by experts that were fully involved in this proceeding, demonstrate that, as a package, the Settlement Agreement is just and reasonable.

For the foregoing reasons, the Settling Parties urge the Commission to approve the Settlement Agreement by order issued on or before June 30, 2006, without any change, deletion or condition.

Respectfully Submitted

ON BEHALF OF THE SETTLING PARTIES,

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UNITED STATES OF AMERICA

BEFORE THE
FEDERAL ENERGY REGULATORY
COMMISSION

Devon Power LLC, et al.) Docket No. ER03-563-___

SETTLEMENT AGREEMENT
RESOLVING ALL ISSUES

(March 6, 2006)

This settlement agreement (the "Settlement Agreement") is entered into by and among the following entities (individually a "Settling Party" and collectively the "Settling Parties"):

American National Power, Inc.
Associated Industries of Massachusetts
Boston Generating, LLC
Calpine Eastern Corporation
Calpine Energy Services, L.P.
Cape Wind Associates, LLC
Central Vermont Public Service Corporation
Connecticut Department of Public Utility Control
The Connecticut Light and Power Company
Connecticut Municipal Electric Energy Cooperative
Connecticut Office of Consumer Counsel
Conservation Services Group

Consolidated Edison Energy, Inc.
Dominion Energy Marketing, Inc.
Dominion Nuclear Connecticut, Inc.
Dominion Resources, Inc.
Duke Energy North America, LLC
Energy Management, Inc.
EnerNOC, Inc.
Entergy Nuclear Generation Company
Entergy Nuclear Vermont Yankee, LLC
Exelon Generation Company, LLC
Exelon New England Holdings, LLC
Fitchburg Gas & Electric Light Company
FPL Energy, LLC
Granite Ridge Energy, LLC
HQ Energy Services (U.S.) Inc.
ISO New England Inc.
Lake Road Generating Company, LP
Long Island Power Authority (LIPA)
MASSPOWER
Milford Power Company, LLC
Mirant Americas Energy Marketing, LP
Mirant Canal, LLC
Mirant Kendall, LLC
Mystic Development, LLC, Mystic I, LLC, and Fore River Development, LLC
National Grid USA (on behalf of itself and its subsidiaries that are intervenors in this proceeding)
NEPOOL Participants Committee
New Hampshire Electric Cooperative, Inc.
New Hampshire Office of Consumer Advocate
New Hampshire Public Utilities Commission

NRG (Devon Power, LLC, Middletown Power LLC, Montville Power LLC, Norwalk Harbor, LLC, and NRG Power Marketing)
Pinpoint Power
Public Service Company of New Hampshire
RI Division of Public Utilities and Carriers
RI Public Utilities Commission
Select Energy
Sempra Trading
TransCanada Power Marketing Limited
The United Illuminating Company
Vermont Department of Public Service
Vermont Public Power Supply Authority
Vermont Public Service Board

The Settling Parties hereby agree as follows:

1. **AGREEMENT REGARDING EFFECTIVENESS.** This Settlement Agreement shall become effective when the Federal Energy Regulatory Commission ("FERC") by order approves this Settlement Agreement in its entirety without modifications or conditions or with such modifications or changes as are agreed to by the Settling Parties in accordance with Section 2 below (the "Effective Date").

2. **AGREEMENT REGARDING TERMINATION.** If the FERC does not approve this Settlement Agreement by June 30, 2006, this Settlement Agreement shall terminate unless the Settling Parties agree to an extension. If the FERC by order approves this Settlement Agreement conditioned on the modification of any of the terms of this Settlement Agreement (a "Conditional Approval Order"), the Settling Parties shall confer and negotiate in good faith to restore the balance of risks and benefits reflected in this Settlement Agreement as executed. Any such renegotiated Settlement Agreement shall be filed with the FERC. If no agreement can be reached within thirty calendar days of the date of the issuance of the Conditional Approval Order and unless all of the Settling Parties agree to extend the time period for such negotiations, this Settlement Agreement shall terminate.

3. **AGREEMENTS REGARDING DEVELOPMENT AND FILING OF MARKET RULES.**

   A. On or before October 1, 2006, the ISO New England Inc. ("ISO"), pursuant to its authority under Section 205 of the Federal Power Act ("FPA"), shall file with the FERC necessary changes to the ISO New England Inc. Transmission, Markets and Services Tariff, FERC Electric Tariff No. 3 (the "Tariff") to implement the Transition Period

as defined in Section 11, Part VIII of this Settlement Agreement. On or before February 15, 2007, the ISO, pursuant to its authority under Section 205, shall file with the FERC necessary changes to the Tariff to implement the Forward Capacity Market as described in Section 11, Parts I through VII and Part IX of this Settlement Agreement.

B. The Market Rules shall be consistent with, and in furtherance of, all the terms contained in this Settlement Agreement as modified by the Settling Parties pursuant to Section 2 of this Settlement Agreement and approved by the FERC. Each Settling Party retains the right to challenge the provisions of the Market Rules that address the terms of this Settlement Agreement only on the basis that they contain provisions that are either inconsistent with or not required by this Settlement Agreement. The Settling Parties retain all rights under the FPA with respect to the provisions of the Market Rules that do not address the terms of this Settlement Agreement.

C. The process for determining the Installed Capacity Requirement ("ICR") for the first Commitment Period shall be reflected in a filing with the FERC in the fourth quarter of 2006 for FERC action, as appropriate, no later than the second quarter of 2007. Such filing shall reflect the understanding that this schedule is intended to enable a filing of the ICR values for use in the first Forward Capacity Auction ("FCA") by early in the third quarter of 2007 for FERC acceptance or approval by October 2007. All Settling Parties retain their rights under the FPA to respond to any such filing.

D. All filings pursuant to this Section 3 shall be subject to the stakeholder process for Market Rules that provides for consultation with state utility regulatory agencies.

4. AGREEMENTS REGARDING CHANGES TO THE SETTLEMENT AGREEMENT AND MARKET RULES.

A. From March 6, 2006 through the earlier of September 5, 2008 or the date on which the prices from the second FCA become final (the "Waiver Period"), the Settling Parties waive their rights under Section 206 of the FPA to seek to modify the terms of this Settlement Agreement or, except as provided in Section 3.B, the Market Rules approved or accepted by the FERC to implement the Forward Capacity Market. Except as provided in Section 4.C, during the Waiver Period, the ISO shall retain its authority under Section 205 of the FPA to file modifications of the Market Rules that address the terms of the Settlement Agreement; where the ISO makes such a filing, the ISO must demonstrate to the FERC that failure to implement the proposed change in the Market Rule would have a negative effect on (1) system reliability or security, or (2) the competitiveness or efficiency of the Forward Capacity Market or forward reserve market. If the ISO makes such a filing, then the Settling Parties shall retain all rights to challenge the modification proposed by the ISO before the FERC.

B. After the Waiver Period, the Settling Parties shall have the rights provided by law with respect to seeking to change this Settlement Agreement or the Market Rules that address the terms of the

Settlement Agreement, except as provided in Section 4.C.

C. From the Effective Date, absent the agreement of all Settling Parties to the proposed change, the standard of review for: (i) challenges to the Capacity Clearing Prices derived through the FCA and prices resulting from reconfiguration auctions provided for in the Settlement Agreement and in the Market Rules addressing the terms of the Settlement Agreement that are approved or accepted by the FERC pursuant to Section 3, and (ii) proposed changes to Section 11, Part VIII below (Agreements Regarding Transition Period) and the Market Rules implementing that part, shall be the "public interest" standard of review set forth in *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332 (1956) and *Federal Power Commission v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956) (the "Mobile-Sierra" doctrine), whether the change is proposed by a Settling Party, a non-Settling Party, or the FERC acting *sua sponte*. This Settlement Agreement does not impose the Mobile-Sierra standard on any provision of this Settlement Agreement or the Market Rules that address the terms of the Settlement Agreement except as expressly provided in this Section 4.C.

5. **AGREEMENTS REGARDING ISO REPORTING.** No later than 180 days after the second FCA is conducted, the ISO's Internal Market Monitoring Unit ("Market Monitor") shall file with FERC and post to the ISO's website a full report analyzing the operations and effectiveness of the Forward Capacity Market. Thereafter, the Market Monitor shall report on the functioning of the Forward Capacity Market in its annual markets report submitted to FERC pursuant to Section 11.3 of Appendix A to Market Rule 1.

6. **AGREEMENTS AS TO SCOPE OF SETTLEMENT.** This Settlement Agreement resolves all of the issues raised in Docket Nos. ER03-563-030 and ER03-563-055 before the FERC by the Settling Parties.

7. **NO ADMISSIONS.** The Settling Parties are entering into this Settlement Agreement to resolve their disputes in Docket Nos. ER03-563-030 and ER03-563-055 before the FERC as specified herein and nothing in this Settlement Agreement, including the January 31, 2006 vote on the term sheet (the "Term Sheet"), is intended by a Settling Party to reflect an admission regarding the merits of its own case or arguments or of another Settling Party's case or arguments on any of the settled issues. Neither support for this Settlement Agreement, nor the Term Sheet relating hereto, nor the submission of this Settlement Agreement and the concurrence in, or failure to comment on, the described settlement, shall constitute an admission by any Settling Party that any allegations or contentions in Docket Nos. ER03-563-030 and ER03-563-055 were true or valid or that any Settling Party had acted consistent with, or contrary to, contract provisions, the FPA, or any other federal or state law or regulation.

8. **CONFIDENTIALITY.** The discussions among the parties related to this Settlement Agreement and the Term Sheet took place within the context of settlement discussions concerning matters covered herein. Discussions leading up to this Settlement Agreement and the Term Sheet, the finalization of this Settlement Agreement and the Term Sheet, and any drafts of those documents, and any other documentation that reflects the negotiation of this Settlement Agreement and the Term Sheet are privileged and confidential in accordance with the applicable sections of

the FERC's Rules of Practice and Procedure, the Federal Rules of Evidence and any other applicable rules of evidence.

9. **ADDITIONAL AGREEMENTS.**

   A. FERC's approval of this Settlement Agreement shall not constitute approval of or precedent regarding any principle or issue in Docket Nos. ER03-563-030 and ER03-563-055 before the FERC.

   B. This Settlement Agreement constitutes the Settling Parties' complete and exclusive statement of the terms of this Settlement Agreement. All prior written and oral understandings, offers or other communications of every kind pertaining to the subject matter of this Settlement Agreement, including without limitation the Term Sheet, are hereby superseded.

   C. This Settlement Agreement may be executed in any number of counterparts, each having the same force and effect as the original.

   D. The Table of Contents contained in this Settlement Agreement and the headings of the sections and parts of this Settlement Agreement are intended for convenience only and shall not be deemed to be part of or considered in construing this Settlement Agreement[.]

10. **DEFINITIONS.** Attachment A to this Settlement Agreement contains a list of all capitalized terms as defined or referenced therein.

11. **AGREEMENTS REGARDING THE ESTABLISHMENT OF A FORWARD CAPACITY MARKET AND TRANSITION.** A Forward Capacity Market shall be established in New England as described in Parts I through VII and Part IX below,

with a transition to that market as provided in Part VIII below.

I. Agreements Regarding the Establishment and Timing of the Forward Capacity Market.

A. Procurement by Forward Capacity Auction and Planning Period. As set forth in and subject to Part I.C (Timing of First Auction) and Part III (Agreements Regarding Auction Mechanics), the ISO shall conduct an annual FCA to procure 100 percent of the ICR for the Power Year beginning three years later, with ICR calculated taking into account forecast error, as appropriate.

B. Commitment Period. Capacity clearing in an FCA shall be entitled to receive capacity payments and shall have the rights and obligations specified below, for a period of either one year in duration (corresponding to the Power Year for which the FCA is held) or up to five years in duration (beginning with the Power Year for which the FCA is held) (the "Commitment Period"), as described in more detail in Part II (Agreements Regarding Qualification).

C. Timing of First Auction. The ISO shall use best efforts to conduct the first FCA no later than the end of the first quarter of 2008 for the first Commitment Period beginning June 1, 2010, and will provide reasonable notice of the first FCA.

II. Agreements Regarding Qualification.

A. Generally. Each potential capacity Resource (Existing, New, or Imports) must submit qualification information to the ISO no later than the relevant bid qualification deadline, which shall be determined during the development of Market Rules. The bid qualification deadline for New Capacity and Imports shall be approximately six

weeks after the ISO's posting of De-list Bids, Permanent De-list Bids and Export Bids from Existing Capacity in accordance with Part III (Agreements Regarding Auction Mechanics).

B. New Capacity. New Capacity may, during the qualification process, select a Commitment Period of up to five years, in one-year increments, provided that the Resource meets the criteria in this Part II.B. New Capacity Resources shall have a Qualified Capacity equal to its bid MWs subject to demonstration of at least that capacity in the qualification process.

1. **Definition of New Capacity.** To be considered New Capacity, a Resource must: (i) never have been "listed" as a capacity Resource (i.e., counted as capacity) in the New England capacity markets; or (ii) meet one of the criteria in Part II.B.2 below.
2. **Thresholds for Previously Listed Capacity to be Considered New Capacity.** A Resource, which had previously been listed as a capacity Resource in the New England capacity markets, shall be considered New Capacity provided it meets at least one of the following conditions:
   a. where new investment in a unit that is Existing Capacity results in an increase in output greater than 20 percent of Summer Seasonal Claimed Capability or 40 MW, whichever is greater.
   b. at owner's election, i) investment in the Resource for the purposes of re-powering will be equal to or greater than $200 (plus appropriate cost escalation) per net kilowatt installed project cost, or ii) investment in

the Resource for the purpose of compliance with environmental regulations or permits will be equal to or greater than $100 (plus appropriate cost escalation) per net kilowatt installed project cost.

c. at owner's election, incremental output from an Existing Capacity Resource shall be considered New Capacity for the incremental amount of output if the output increase is equal to or greater than two percent of the Resource's Summer Seasonal Claimed Capability, but less than the requirements in part a. above. Additionally, if Existing Capacity is derated for three or more years, any capacity over the derated amount that is re-established shall be considered New Capacity. Provided, however, that investment in the Resource for such purposes shall be equal to or greater than $200 (plus appropriate cost escalation) per net kilowatt installed cost for the incremental output.

d. additional thresholds for New Capacity treatment may be addressed in the stakeholder process that provides for consultation with state utility regulatory agencies (e.g., new source environmental review and Resources with a new "placed in service date" for purposes of Section 45K (formerly Section 29) of the Internal Revenue Code of 1986).

3. **Eligibility Criteria.** In order for any Resource to be eligible to bid in the FCA as New Capacity, including to the extent applicable New Capacity under Parts II.B.2, it must meet

the qualification requirements listed in a. through d. below to the satisfaction of the ISO. Qualification criteria may vary based on the size, technology, complexity, et cetera of the Resource. Such qualification requirements shall be further detailed as part of the development of Market Rules. A New Resource that intends to submit a New Capacity Bid below 0.75 the Cost of New Entry ("CONE") shall submit sufficient information for the Market Monitor to evaluate the reasonableness of the bid consistent with Part III.H.2.

a. Site Control. The project sponsor shall demonstrate that it has control over the site for its project over the term of the intended Commitment Period, by providing documentation to the ISO showing that (i) the project sponsor is the owner in fee simple of the real property on which the project will be located; (ii) the project sponsor holds a valid written leasehold interest in the real property on which the project will be located; (iii) the project sponsor holds a valid written option, exercisable solely by the project sponsor or its assignee, to purchase or lease property on which the project will be located; or (iv) the project sponsor holds a duly executed written contract to purchase or lease the real property on which the project will be located.

b. Critical Path Schedule. The project sponsor must provide a critical path schedule for their project with sufficient detail to allow the ISO to evaluate the feasibility of the project being built and the feasibility

that it will be put into service no later than the start of the Commitment Period, as set forth in Part II.B.4.

c. Interconnection Study. If applicable for a specific Resource, while a full and complete System Impact Study is not a requirement to participate in the FCA, at a minimum, an initial interconnection analysis is required. The ISO and the Reliability Committee shall work out specifics with respect to the performance of such initial interconnection analysis and selection criteria (including auction details) for multiple projects when only a subset of such projects can be selected in the FCA due to overlapping interconnection impacts.

d. Financial Assurance. Bidders must satisfy the Financial Assurance requirements for New Capacity specified in Part II.G.

4. **Milestone Criteria.** For purposes of consideration as New Capacity in the FCA, several key milestone dates shall be included in a critical path schedule as a means of demonstrating that the Project will come on-line prior to the delivery date for the relevant Commitment Period. The ISO shall evaluate the milestone schedule for reasonableness in accordance with processes defined in development of the applicable FCA Market Rules. The key milestone dates may include:

a. Site control achieved;

b. Major permits applied for;

c. Major permits obtained;

d. Construction financing closing;

e. Interconnection Study completed;

f. Equipment ordered;

g. Foundations laid;

h. Commencement date of operations.

5. **Timing.** A Resource intending to participate in an annual FCA as New Capacity must submit its qualification package before the start of the FCA at a time to be determined in the Market Rules.

C. Import and Export Capacity. Import Capacity bids shall only be eligible for a one-year Commitment Period, and qualification requirements shall depend on whether the Import Capacity is committed under a multi-year contract prior to the qualification deadline. The qualification deadline for Import Capacity shall be the same as for New Capacity, and the qualifications deadline for an Export Bid shall be the same as for an Existing Capacity De-list Bid.

1. **Definitions of Import and Export Capacity.**

a. **Existing Import Capacity.** Capacity that a party wishes to import in the FCA pursuant to a multi-year contract entered into before the qualification deadline to provide capacity Resources during the Commitment Period from outside the New England Control Area shall be Existing Import Capacity and shall be considered Existing Capacity for purposes of Part III.D. Provided, however, that during the first year of a multi-year contract such Existing Import Capacity in the FCA shall be considered New Import Capacity for purposes of Part III.D. Multi-year contracts existing as of

the Effective Date will be treated as Existing Capacity for the purposes of the first FCA.

b. **New Import Capacity.** Capacity that a party wishes to import in the FCA but without a multi-year contract before the qualification deadline to provide capacity Resources during the Commitment Period from outside the New England Control Area shall be New Import Capacity and shall be considered New Capacity offers for purposes of Part III.D.

c. **Export Capacity.** Any Resource within the New England Control Area seeking to submit a bid to export all or part of its capacity in the FCA or selling its De-listed Capacity to a buyer outside the Control Area following the FCA shall be Export Capacity. Only the portion of the Resource seeking to export shall be Export Capacity.

2. **Eligibility Criteria.**

a. In the qualification process, Existing Import Capacity bidders must submit to the ISO documentation of a multi-year contract to provide capacity Resources for the Commitment Period and must meet the same eligibility criteria specified in Part II.D.2.a., b., and e. for Existing Capacity, including the Financial Assurance Requirements for Existing Capacity in Part II.G.2.a.

b. New Import Capacity Resources must meet the qualification requirements listed in i. and ii. below to the satisfaction of the

ISO. Such qualification requirements shall be further detailed as part of the development of Market Rules. New Import Capacity that intends to submit a bid below 0.75 CONE must also submit sufficient information for the Market Monitor to evaluate the reasonableness of the bid consistent with Part III.H.2.

i. New Import Capacity bidders must comply with Market Rules that require the New Import Capacity to be backed by a physical unit or an external control area before the start of the Commitment Period.

ii. New Import Capacity bidders must satisfy all of the Financial Assurance requirements for New Capacity specified in Parts II.G.2.b and c.

c. Export Capacity Resources must meet the same eligibility criteria as applied to Existing Capacity in Part II.D.2.b. Export bids are subject to review by the Market Monitor, as provided for Existing Capacity in Parts III.D.2 and III.E.

D. **Existing Capacity.** Existing Capacity shall have a Commitment Period of one year. An Existing Capacity Resource will have a Qualified Capacity for the FCA and annual reconfiguration auctions, except as provided in Part II.D.5, equal to its Summer Seasonal Claimed Capability as adjusted pursuant to Part II.D.4. below. All Existing Capacity shall be a capacity Resource in the FCA unless its Export, De-list, or Permanent De-list Bid is accepted or it submits an Administrative De-list Bid. With its information submitted for qualifica-

tion, Existing Capacity must submit all Export, De-list and Permanent De-list Bids, other than Dynamic De-list Bids. Bids from Existing Capacity may be reviewed by the Market Monitor, as discussed below. The Market Rules that address the terms of this Settlement Agreement shall provide a means for Existing Capacity to trade or de-list (subject to a reliability review if required) the capacity differential between the summer and winter ratings, including trading contemplated by Part III.M.7 and Part III.P, unless sold in the FCA pursuant to Part II.D.5 below.

1. **Definition of Existing Capacity.** Any Resource that does not meet any of the eligibility criteria for New Capacity as provided in Part II.B.3 or Import Capacity as provided in Part II.C.2.a or b. shall be considered to be Existing Capacity. Subject to ISO evaluation, for the purposes of the first FCA, any Resource that is under construction and within 12 months of its expected commercial operations date shall be treated as Existing Capacity. Any Resource that is not within 12 months of its expected commercial operations date at the time of the first FCA shall be treated as New Capacity, unless the Resource is required pursuant to contract or otherwise elects to be treated as Existing Capacity.
2. **Eligibility Criteria.** Existing Capacity must submit documentation of the following as part of a qualification package:
    a. A Resource that is not submitting Export, De-list, or Permanent De-list Bids shall submit documentation as required by the Market Rules.

b. A Resource that intends to submit an Export, De-list, or Permanent De-list Bid above 0.8 CONE in the FCA shall submit sufficient documentation for the Market Monitor to evaluate the bid pursuant to Part III.E.

c. A Resource that intends to submit a Permanent De-list bid in the FCA shall submit sufficient documentation for the Market Monitor to evaluate the bid pursuant to Part III.E., and for the ISO to evaluate the reliability impact of the permanent delisting.

d. A Resource seeking to qualify as New Capacity in accordance with Part II.B.2 above, for either an incremental amount or for the full output of the Resource, shall be required to submit documentation in support of its request for New Capacity treatment. The ISO shall evaluate this documentation in accordance with the Market Rule provisions to validate the request for New Capacity treatment.

e. Financial Assurance. Bidders must satisfy the Financial Assurance requirements for Existing Capacity specified in Part II.G.

3. **Timing.** An Existing Capacity Resource intending to submit any Export, De-list, Permanent De-list, or Administrative De-list Bid (other than a Dynamic De-list Bid) in the FCA as Existing Capacity must submit its qualification package before the start of the FCA, at a time to be determined in the Market Rules.

4. **Partial Delisting.** An Existing Capacity Resource may submit De-list Bids for all or part of its Existing Capacity, provided that the portion of the unit which it chooses to "list" is at least equal to the EcoMin level of the unit.
5. **Bids Composed of Separate Resources.** An annual bid can be composed of separate Resources in different months, if the Resources together, based on their monthly ratings, can meet or exceed the amount of the offer throughout the year, and subject to the following conditions in subparts 5.a through 5.f below. In the Winter Period, Resources may use Summer Seasonal Claimed Capability not taken in the annual FCA or the difference between their Winter and Summer Seasonal Claimed Capability, provided that under no circumstances can the same MWs be counted twice in the same FCA.
    a. If a bid is composed of separate Resources, and is intended to meet the "Local Sourcing Requirement" in an import-constrained Capacity Zone[,] then each Resource comprising the bid must be located in that import-constrained Capacity Zone. Local Sourcing Requirement means the portion of the total capacity requirement of the load in a Capacity Zone that must be purchased from Resources located within that Capacity Zone after taking into account all of the capacity that can be reliably imported into the Capacity Zone.
    b. If a bid is composed of separate Resources, and is intended to meet the Local Sourcing Requirement in the Rest-of-Pool Capacity

Zone, then each Resource comprising the bid must be located in a Capacity Zone that is not export-constrained.

c. If a bid is composed of separate Resources, and is for capacity in an export-constrained Capacity Zone, then each Resource comprising the bid must be located inside the export-constrained Capacity Zone.

d. Bids cannot be composed of separate Resources for the same month.

e. A bid composed of separate Resources shall be treated for purposes of clearing in the FCA or a reconfiguration auction as New Capacity, Existing Capacity, or Import based on the Resource providing summer capacity.

f. In instances where the export constraint for a Capacity Zone binds in the FCA, and such an offer is accepted within that Capacity Zone, Part V.C.4.c shall not apply to such capacity Resource.

E. Intermittent and Demand Resources.

1. **Intermittent Resources.**

a. For the Forward Capacity Market, a distinct method shall be developed to determine the Qualified Capacity of wind, solar and run-of-river hydro resources ("Intermittent Resources") in a manner that recognizes contribution to system reliability over the Winter and Summer Periods. So that it can be appropriately considered in the ICR determinations for the Forward Capacity Market, such method shall be developed by the end of the fourth quarter of

2006 through the stakeholder process that provides for consultation with state utility regulatory agencies. Intermittent technology resources other than wind, solar and run-of-river hydro resources may request to be considered in the definition of Intermittent Resources for purposes of this part provided that such resources remain subject to the same method for determining Qualified Capacity. Any such request shall also be subject to the stakeholder process that provides for consultation with state utility regulatory agencies.

b. The process described above for developing a methodology for determining the Qualified Capacity of an Intermittent Resource shall also consider how to address poorly performing Intermittent Resources, since these types of Resources are not subject to availability penalties and/or poor performing Resource treatment as other Resources. The Market Rules will address how Intermittent Resources will be defined as New Capacity in the FCA.

2. **Demand Resources.**

a. In the Forward Capacity Market, Real Time Demand Response shall remain as qualifying capacity Resources subject to Market Rule 1, Appendix E and the Load Response Manual. As such, the role of demand response Resources in the market shall continue to evolve as Market Rule 1, Appendix E and the Load Response Manual are revised.

b. For the Forward Capacity Market, a distinct method shall be developed to allow energy efficiency and demand response resources (other than Real Time Demand Response) to be fully integrated as Qualified Capacity in the Forward Capacity Market. So that it can be appropriately considered in the ICR determination for the Forward Capacity Market, such method shall be developed by the end of the fourth quarter of 2006 through the stakeholder process that provides for consultation with state utility regulatory agencies. The method shall consider that some Resources may best be integrated by ensuring that price signals are correct. Such Qualified Capacity shall not be subject to the same availability penalties and/or poorly performing Resource treatment as other Resources, so the method shall also propose how to address poorly performing demand response and energy efficiency Resources. The Market Rules will address how demand Resources will be defined as New Capacity in the FCA.

F. Self-Supplied FCA Resources.

1. **Qualification.** Prior to each FCA, a Resource or a portion of a Resource may be designated by a Load-Serving Entity ("LSE") pursuant to Market Rules as a self-supplied FCA Resource ("Self-Supplied FCA Resource"). The Self-Supplied FCA Resource must meet the same qualification standards as any other Resource that is allowed to participate in the FCA. The total quantity of designated Self-Supplied FCA

Resources may not exceed the projected share of the ICR for the LSE designating that Resource pursuant to Market Rules. To be considered a Self-Supplied FCA Resource, that Resource must be offered into the FCA. If designated as a Self-Supplied FCA Resource, the Resource will clear the FCA pursuant to Part III.O (Agreements Regarding Auction Mechanics – Self-Supply Option) and offset an equal number of megawatts of the projected share of ICR in the Commitment Period for the LSE designating that Resource.

2. **Locational Issues.** In order to qualify as a Self-Supplied FCA Resource for purposes of fulfilling a Local Sourcing Requirement applicable to a load in an import-constrained region, the Self-Supplied FCA Resource must be located in the same Capacity Zone as the associated load, unless the self-supplied resource is a Pool-Planned Unit with a special allocation of Capacity Transfer Rights ("CTRs") up to the number of allocated CTRs. Although the ISO will continue to model any such Pool-Planned Units in their actual location, the combination of the physical asset and the CTRs will offset the financial obligation of the self-supplier.

G. Financial Assurance. The following general requirements shall apply to the FCA and annual reconfiguration auctions. Except where noted, the retention and return of financial assurance and the types of acceptable financial assurance will be governed by the Financial Assurance Policy ("FAP"). Financial assurance requirements for Municipal Market Participants will be consistent with Section III of the FAP.

1. **Load-Serving Entity Obligation.** The financial assurance requirement for capacity payments for each month of the Commitment Period will be equal to the amount that represents the actual credit exposure of the LSE (e.g., the amount due from the LSE obligated to make those payments on the next invoice to be issued by the ISO).
2. **Supplier Obligation**
   a. Existing Capacity: Existing Capacity generally shall be subject to the Financial Assurance requirements contained in the FAP. In addition, except where the capacity obligation has been transferred to another Resource, Existing Capacity that has been allowed to retire under Section I.3.9 of the Tariff and will retire at the end of the relevant Commitment Period shall be required to provide additional financial assurance equal to two and one-half times the FCA Payment for a month. The financial assurance obligation under this part shall arise five business days before the start of the applicable Commitment Period, and the Financial Assurance shall be returned in accordance with the FAP.
   b. New Capacity: In order to submit a bid in an FCA, New Capacity must be qualified pursuant to Part II.B.3 above and provide financial assurance at the time of its qualification (the "Deposit") equal to $2/kW times the amount of kilowatts to be bid as New Capacity into the FCA. If that New Capacity's bid is accepted in the FCA, the Deposit will be applied toward the New

Capacity's financial assurance obligation, described below. If that New Capacity bid is rejected, the Deposit will be returned to the New Capacity. New Capacity that receives an award in an FCA must provide financial assurance in the following amounts:

i. Within five business days following announcement of the winning bidders: the CONE (on a $/kW-month basis) for that FCA multiplied by the number of kW of capacity awarded (the "New Capacity FA Amount");

ii. At least fifteen days prior to the next annual FCA after the FCA in which such award was made: an additional amount equal to the New Capacity FA Amount (for a total of two times the New Capacity FA Amount); and

iii. At least fifteen days prior to the second annual FCA after the FCA in which such award was made: another additional amount equal to the New Capacity FA Amount (for a total of three times the New Capacity FA Amount).

The New Capacity FA Amount for the first FCA will be $7.50 per kW, as provided in Part III.F[,] and shall be updated annually before each FCA in accordance with Part III.F. Therefore, for example, a new 100 MW generating unit that has a bid accepted as New Capacity in the first FCA would have to provide $750,000 of financial assurance within five days following an-

nouncement of the winning bidders. That unit would have to provide another $750,000 of financial assurance at least fifteen days prior to the FCA the following year (for a total financial assurance obligation of $1,500,000). That unit would have to provide another $750,000 at least fifteen days prior to the next FCA (for a total financial assurance obligation of $2,250,000).

If New Capacity (i) fails to provide the required financial assurance on any required date for any reason or (ii) fails to meet a qualification milestone as set forth in Part II.B.4 and does not appropriately cure such failure within a period of time to be determined in the Market Rules, it shall lose its awarded capacity to the extent not provided (which will be placed in the next appropriate reconfiguration auction) and it shall forfeit any financial assurance previously provided by it with respect to that award. The ISO and the NEPOOL Budget and Finance Subcommittee shall reconsider these financial assurance requirements no later than five years after the first FCA.

iv. Once the New Capacity is declared commercial and tested for its capacity rating, its financial assurance obligation shall be released and it shall have the same financial assurance requirements as Existing Capacity. If New Capacity is only capable of delivering

less than the amount accepted in the FCA, then the portion of its financial assurance associated with the shortfall shall be forfeited.

v. A default before the relevant Commitment Period or a failure to be declared commercial as of the Commitment Period, if not cured (including cover)[,] shall result in a forfeiture of the financial assurance, and there shall be no further coverage for such default under the Billing Policy. Such forfeited amount shall be used to reduce capacity payments by load. Any shortfall in capacity resulting from a default shall be included in a subsequent reconfiguration auction. If New Capacity is not commercial as of the Commitment Period, it shall have the right to cover the default for a period of up to two years. After such a period, following consultation between the Resource and the ISO, the ISO shall have the right to terminate the Resource's award under the FCA for the remaining portion of the Commitment Period and, at the same time[,] terminate the Interconnection Agreement. The ISO shall make a filing with the FERC reflecting such terminations. Should New Capacity challenge such termination at FERC and also continue to cover its default, then it shall retain its place in the queue and forfeiture of its financial

assurance shall be subject to a final FERC ruling[.]

c. Financial assurance requirements for imports will be covered in the Market Rules in a manner that is consistent with Part II.C.2 above and II.G.2.b. New Import Bids will meet New Capacity financial assurance requirements until the New Import Capacity is backed by a physical unit or an external control area, and thereafter it shall have the same financial assurance requirements as Existing Capacity.

3. **Price and Payment Certainty and Finality.**

a. The capacity delivery obligations of suppliers, the payment obligations of LSEs and the FCA process and rules shall be documented in the Tariff. The Tariff shall include language stating that a change in the Tariff filed after FCA results have been accepted or approved by the FERC will not change those FCA results and also documenting terms and conditions consistent with this Settlement Agreement that apply to capacity clearing in the FCA for the Commitment Period of that FCA, including at a minimum the following: (i) payment terms (timing, immediately available funds, process for disputed payments); (ii) financial assurance requirements; (iii) events of default and other events that could lead to termination of the obligations or suspension of capacity payments; (iv) the right for New Capacity, or its lender(s) if applicable, to cure a default (including any default resulting from bankruptcy of the owner of

New Capacity), which in the case of a lender cure would not require the lender to become the owner of the plant; (v) notice of any event of default to the owner of New Capacity and its lender(s); (vi) the capacity obligations imposed on the New Capacity and means for determining whether such obligations have been satisfied; (vii) damages to be paid in event of failure to perform and recourse for non-payment; and (viii) the right for the New Capacity owner to pledge moneys due to New Capacity to lenders and to direct payment of such moneys into a project revenue account and that other Rights of New Capacity owners can be pledged. The Tariff shall also provide that an award in a FCA is binding upon, and accrues to the benefit of, successors and assigns owning that Resource.

b. The ISO shall promptly file the FCA results including the detail of the awards and the price, together with appropriate documentation as to the competitiveness of the FCA, with the FERC under Section 205, or make such other filing as is necessary to establish the FCA results as filed rates. Any objection to those results must be filed with the FERC within 45 days after the ISO's filing. The filing of a timely objection at the FERC will be the exclusive means of challenging the FCA results.

"Appropriate documentation as to the competitiveness of the FCA" may include, but may not necessarily be limited to, the certification of the Auction Administrator

(whether the ISO or a contractor [is] engaged for that purpose), that (i) all bidders in the FCA have satisfied the qualification requirements established in the Tariff and applicable Market Rules and Manuals and business practices issued in accordance therewith, and (ii) that the FCA was conducted in accordance with the applicable rules and procedures. Further detail to be developed in the Market Rules.

4. **Default Allocation.** To the extent that any default is not cured (including in the reconfiguration auction), any resulting cash shortfall shall be allocated according to the Billing Policy.

III. Agreements Regarding Auction Mechanics.

A. Zonal Selection Criteria and Locational Pricing. Capacity Zones shall be defined in advance of each FCA.

1. Capacity Zones shall be determined before the FCA based on an identification of transmission limits that may bind in the FCA.
2. Transmission interface limits used in the process of selecting Capacity Zones shall include all existing transmission lines and proposed transmission lines that the ISO determines will be in service as of the relevant Commitment Period.
3. Before the start of each FCA, the then-forecasted capacity installed in a Capacity Zone, including Resources (Existing Capacity, New Capacity and Import Capacity accepted in prior FCAs or reconfiguration auctions and obligated for the relevant Commitment Period), less Permanent De-list Bids accepted in prior

FCAs and Export Bids accepted in prior FCAs and obligated in the Commitment Period, shall be compared to the Zone's then-forecasted Local Sourcing Requirement in the first year of the Commitment Period.

For the first FCA, any entity that believes capacity under construction will be complete for the first Commitment Period and therefore should be included in the process of selecting Capacity Zones must satisfy the eligibility criteria, where applicable, of Part II.B.3.

4. For an import-constrained zone, if the then-forecasted capacity, including Resources (Existing Capacity, New Capacity and Import Capacity obligated for the relevant Commitment Period), less Permanent De-list Bids accepted in prior FCAs and Export Bids accepted in prior FCAs and obligated in the Commitment Period in the zone is greater than its then-forecasted Local Sourcing Requirement before the start of each FCA, the zone shall not be a separate zone in the FCA.
5. Export-constrained zones are modeled in the FCA.
6. Where zonal separation is determined to exist, CTRs shall be awarded as set forth in the Initial Decision, provided that any special allocation of CTRs to LSEs in the NEMA zone shall expire on December 31, 2040. In the event that the NEMA zone either is or is forecast to become a separate zone for FCA purposes, National Grid agrees to discuss with MMWEC and Wellesley, Reading and Concord ("WRC") any proposal by National Grid to develop cost effective transmission improvements that

would mitigate or alleviate the import constraints and to work cooperatively and in good faith with MMWEC and WRC regarding any such proposal. MMWEC and WRC agree to support any proposals advanced by National Grid in the Regional System Planning ("RSP") process to construct any such transmission improvements, provided that MMWEC and WRC determine that the proposed improvements are cost effective (without regard to CTRs) and will mitigate or alleviate the import constraints.

7. Changes to the definition of zones shall be subject to the stakeholder process that provides for consultation with state utility regulatory agencies.

8. Where zonal separation is determined to exist, Market Rules shall specify a process for an Export both from or through the import-constrained zone over tie lines to external regions.

B. Installed Capacity Requirement. Subject to Section 3.C, each year, in advance of the FCA, the ISO shall submit to FERC for acceptance or approval the ICR for the New England system and the Local Sourcing Requirement for each year for each Capacity Zone, accounting for relevant transfer limits, through the Power Year beginning three years later. The ICR purchased shall be based on the Summer Seasonal Claimed Capability. Capacity to meet the ICR shall be based on that Resources' Summer Seasonal Claimed Capability except for Resources specified in Parts II.D.4, II.E, and VI (regarding external Resources).

1. ICR will be calculated taking Resource availability into account. As experience permits, the availability metric in Part V.C. below will be incorporated.
2. If the ICR shows a consistent bias over time, either high or low, the ICR forecast process shall be adjusted to eliminate the bias.
3. The ICR shall be calculated assuming appropriate tie benefits, if any, from adjacent control areas.
    a. The MW value of the tie benefits over the HQ Phase I/II tie will continue to be calculated in the manner that is currently used to determine the Hydro Quebec Interconnection Capability Credits ("HQICCs") and will also continue to be allocated to the Interconnection Rights Holders ("IRH") or their designees in proportion to their Use Rights, in the form of reduced capacity requirements. There shall be no double counting of the HQ Phase I/II tie benefits. This calculation and allocation methodology of the HQ Phase I/II tie benefits will continue unless and until a modification thereto is accepted by the FERC, provided that nothing in this Settlement Agreement, specifically including this section, Part III.D.4.a and Part VIII.K., will constitute precedent regarding the reasonableness of (i) such modification, or (ii) the manner of calculating or allocating the Phase I/II tie benefits. Nothing in this Settlement Agreement prejudices the rights of any party to seek to modify or challenge the calculation or allocation methodology of HQ

Phase I/II tie benefits for the period beginning after the end of the Transition Period, as defined in Part VIII.A.

b. The total amount of accepted Import Bids over the Phase I/II tie plus approved HQICCs cannot exceed the approved Phase I/II transfer limit. If the accepted Import Bids exceed the difference between the approved Phase I/II transfer limit and the approved MW of HQICCs (the "HQI Excess"), the capacity requirement for those IRH or their designees that sold their transmission rights for the subject period will be increased by the difference between the total amount of accepted Import Bids and the HQI Excess. These capacity requirement increases will be allocated among the IRH or their designees in a manner to be determined by the IRH.

C. Amount of Capacity Purchased. One hundred percent of the ICR, taking into account forecast error, as appropriate, except in certain instances where capacity to replace Export Bids, Permanent De-list Bids and De-list Bids is deferred to the reconfiguration auction (see Part III.D.2-3, and D.5), will be purchased in the FCA at prices up to two times CONE, subject to Part III below.

D. Forward Capacity Auction Offers.

1. **New Capacity Offers.** All offerors of New Capacity must satisfy the applicable requirements of Part II.B. In order to receive capacity payments during the Commitment Period, New Capacity must have been declared commercial and tested for its capacity rating.

2. **Offers From Existing Capacity.** All Existing Capacity must submit appropriate information in the qualification process as described in Part II.D.2. All De-list Bids above 0.8 times CONE from Existing Capacity, all Export Bids, and all Permanent De-list Bids must be submitted to the ISO before the bid qualification deadline to be considered in the FCA. All Permanent De-list and De-list Bids from Existing Capacity that are above 0.8 times CONE must also be submitted to the Market Monitor before the bid qualification deadline to be considered in the FCA. Full information about Permanent De-list Bids will be posted one day after the bid qualification deadline.

   The quantity, price and zone of each De-List Bid above 0.8 times CONE will also be posted one day after the bid qualification deadline; if the bid is approved by the Market Monitor, full information will be posted. Authorized Persons of Authorized Commissions, as defined in Section 3.3 of the ISO New England Information Policy, will be provided confidential access to full information about posted De-list Bids upon request pursuant to Section 3.3 of the Information Policy.

3. **Permanent De-list Bids.** A Permanent De-list Bid shall be accepted if the Capacity Clearing Price falls below the Permanent De-list Bid price. If a capacity Resource's Permanent De-list Bid is accepted, the Resource shall not be eligible to receive Capacity Payments in the Commitment Period associated with the FCA or any subsequent FCA or reconfiguration auction, until such time as the Resource may meet the qualifications for New Capacity for a

subsequent FCA. If a capacity Resource's Permanent De-list Bid is accepted, that Resource may still participate in all other markets according to the rules of those markets.

a. **Capacity to Replace Permanent De-lists.** Capacity needed to replace the capacity associated with an accepted Permanent De-list Bid shall not be purchased in the FCA if the Capacity Clearing Price equals or exceeds 1.5 times CONE. Instead, the full amount of capacity requirement resulting from such accepted Permanent De-list Bids shall be advanced into subsequent reconfiguration auctions.

   i. For prices between 1.25 times CONE and 1.5 times CONE, the quantity of capacity requirement associated with Permanent De-lists replaced in the FCA increases pro-rata. The amount of capacity needed to replace capacity of an accepted Permanent De-list Bid that is not purchased in the FCA shall be purchased in subsequent reconfiguration auctions.

   ii. Permanent De-list Bids below 1.25 times CONE shall be eligible to set the price in the FCA. If accepted, the capacity requirements shall be replaced in full in the FCA.

4. **Import and Export Bids.** Full information about Import and Export Bids (name of submitter, quantity and interface) shall be published the day after offers are submitted.

a. **Imports.** The sum of the tie benefits plus imports over the New York interface cannot exceed the approved transfer limits of the interface for the Forward Capacity Market. Similarly, the sum of the tie benefits plus imports over the New Brunswick interface cannot exceed the approved transfer limits of the interface for the Forward Capacity Market. Imports treated as capacity must become physical (i.e., backed by a physical unit or an external control area) prior to the time of delivery and must meet the same or comparable performance requirements as other capacity Resources in order to receive capacity payments.

   The current capacity treatment within NEPOOL of firm imports of New York Power Authority ("'NYPA") hydroelectric power, which is set forth in Section 3.4 and Appendix A of NEPOOL Manual No. 20 for Installed Capacity, shall be continued, such that NYPA firm import allocation recipients will be able to continue to claim capacity credit for these firm imports during the transition, in as close as possible a manner to its treatment today.

   Imports shall be allowed over interfaces until the sum of the tie benefits plus imports equals the approved transfer limits on the relevant interface or the descending clock stops.

b. **Exports.**

   i. Export Bids offered into the FCA will be treated the same as De-list Bids ex-

cept that they must also indicate the interface over which the capacity will be exported (e.g., Cross Sound Cable, Rest of Pool to New York, HQ Phase I and II, HQ Highgate, and New Brunswick). In assessing the reasonableness of an Export Bid, the Market Monitor shall take appropriate consideration of contracts and the revenue opportunities of Resources bidding to export.

ii. Capacity needed to replace the capacity associated with an accepted Export Bid shall be treated the same as capacity associated with an accepted De-List Bid under Part III.D.5.a below.

iii. Exports shall be allowed over interfaces until the interface limit constraints bind or the descending clock stops.

iv. Exporting capacity, which has been accepted in a prior FCA or contracted prior to the implementation of the FCA, may Administratively De-list in the qualification process by demonstrating a contractual obligation to sell capacity outside of the New England Control Area for the Commitment Period. This action will be reviewed by the Market Monitor pursuant to rules to be developed.

v. Export Bids are subject to rationing to the extent the external interface binds.

5. **De-list Bids.** Existing Capacity wishing to opt out of the capacity market in the Commitment Period may submit a De-list Bid. Such Resources may offer capacity in reconfiguration FCAs. If a capacity Resource's De-list Bid is accepted, that Resource may still participate in all other markets according to the rules of those markets.
    a. **Capacity to Replace De-lists.** Capacity needed to replace the capacity associated with an accepted De-list Bid above 1.2 times CONE shall not be purchased in the FCA. Instead, the capacity needed to replace the capacity associated with such De-list Bids shall be advanced into subsequent reconfiguration auctions. For prices from 0.8 times CONE to 1.2 times CONE, the quantity of replacement capacity for accepted De-list Bids purchased in the FCA increase pro-rata. Any De-list Bids that were not purchased in the FCA shall be purchased in a reconfiguration auction.
    b. **Dynamic De-list Bids.** During any round of the descending clock FCA, any existing Resource may offer to de-list all or a portion of its capacity (including a partial De-list Bid) if the De-list Bid is offered at or below 0.8 times CONE. Such an offer is eligible to set the Capacity Clearing Price. If more De-List Bids are submitted at a price than are needed to clear the market, the ISO shall accept these De-List Bids pro-rata.
6. **Rationing Rule.** Project-specific bids from New Capacity and unit-specific bids from Ex-

isting Capacity and Existing Import Capacity must be taken or rejected in whole unless the bidder has specified otherwise. Existing Capacity may structure bids to partially de-list or export all or a portion of a Resource. Market clearing shall be based on minimizing total FCA costs for the first year of the Commitment Period. Import Bids are subject to rationing, subject to technical limits on minimum delivery.

E. **Review by Market Monitor.** In reviewing bids from Existing Capacity that are subject to review as set forth in Part III.D above, the Market Monitor shall review that the proposed bid is consistent with the Resource's net risk-adjusted going-forward and opportunity costs, recognizing, among other things, infra-marginal rents, availability adjustments, and PER deductions. Provided, however, that Permanent De-list Bids below 1.25 times CONE shall be presumed competitive unless the Market Monitor determines that the bid is an attempt to manipulate the FCA. The details of this review shall be developed in the Market Rules.

The Market Monitor shall have the authority to review all offers below Summer Seasonal Claimed Capability to assure that they are not attempts to exercise physical withholding. The details of this review shall be developed in the Market Rules. The Market Monitor shall also have authority to review all Import Bids to assure that they are not attempts to manipulate the FCA, and the details of this review shall be developed in the Market Rules.

Where an entity submits both a New Capacity bid and a De-list Bid in the same FCA, the Market Monitor shall take appropriate steps to ensure that the unit de-listed in the FCA is not inappropriately substituted for the New Capacity Resource in subsequent reconfiguration a[u]ctions.

New Capacity and New Import Bids below 0.75 times CONE are subject to Market Monitor review as described in Part III.H. below.

F. Starting Price and Determination of CONE. The first round of the descending clock FCA shall have a starting price of 2 × CONE, with CONE initially set at $7.50/kW-month (therefore, the initial starting price will be $15). Following the third FCA that has not been found to have Insufficient Competition or Inadequate Supply ("Successful FCA"), CONE will be based on the historical average capacity price using exponential smoothing with a parameter of 30 percent. That is,

CONE in year t + 1 =

(70% of CONE in year t) + (30% of Capacity Clearing Price in year t),

with the exception that if the FCA failed in year t (either due to Insufficient Competition or Inadequate Supply) or if no new entry is required, or if Imports set the Capacity Clearing Price, or if the New Capacity bids in Part II.B.2.c set the Capacity Clearing Price (incremental additional capacity that is treated as new) then

CONE in year t + 1 = CONE in year t.

Approach to be applied to determine CONE before three Successful FCAs:

Year 1 (First FCA): $7.50/kW-month.

Years following the first Successful FCA but prior to the second Successful FCA: $3.75/kW-month (50% of $7.50) plus 50% of the Successful FCA Capacity Clearing Price.

Years following the second Successful FCA but prior to the third Successful FCA: $1.88/kW-month (25% of $7.50) plus 75% of the average of the two previous Successful FCA Capacity Clearing Prices.

G. Capacity Clearing Price.

1. A single run of the descending clock FCA shall establish the Capacity Clearing Price for each Capacity Zone based on the amount of capacity procured as described above. Permanent De-list Bids, Import Bids, Export Bids, and De-list Bids shall be eligible to set the Capacity Clearing Price subject to the limitations described above. Permanent De-list Bids and De-list Bids that are rejected for reliability reasons are not eligible to set the Capacity Clearing Price.
2. For prices below 0.8 times CONE, the full ICR, including capacity associated with all cleared Permanent De-list and De-list Bids, shall be covered in the FCA. For prices between 1.25 times CONE and 1.5 times CONE, the quantity of Permanent De-lists covered in the FCA shall increase linearly. At 1.5 times CONE, no Permanent De-list Bids above that level shall be covered in the FCA; at 1.25 times CONE, all Permanent De-list Bids shall be covered. Similarly, for prices from 0.8 times

CONE to 1.2 times CONE, the quantity of De-list Bids covered in the FCA shall increase linearly. At 1.2 times CONE, no De-list Bids shall be covered; at 0.8 times CONE, all De-list Bids above that level shall be covered.

3. In an import-constrained Capacity Zone, the Capacity Clearing Price shall always be at least as high as the Capacity Clearing Price in the Rest of Pool Capacity Zone.

4. For the lesser of five FCAs or three Successful FCAs: (a) if the Capacity Clearing Price is above 1.4 times CONE, Existing Capacity shall be paid 1.4 times CONE, and New Capacity shall be paid the Capacity Clearing Price; and (b) the Capacity Clearing Price shall not fall below 0.6 times CONE. At 0.6 times CONE, any excess supply shall be prorated to procure no more than ICR, as follows: the total payment to all listed Resources shall be equal to 0.6 times CONE times ICR. Payments to listed individual Resources shall be prorated based on the total number of bid MWs of listed units. Suppliers wishing instead to prorate their bid MWs of participation in the capacity market can do so by partially de-listing one or more Resources in their portfolio (or an equivalent mechanism to be developed in the Market Rules) after the need for proration is identified.

H. New Capacity and New Import Bids below 0.75 CONE.

1. New Capacity and New Import Bids below 0.75 times CONE must be submitted to the Market Monitor before the bid qualification deadline to be considered in the FCA.

2. If the Market Monitor finds that the New Capacity Bid below 0.75 times CONE is consistent with the long run average costs of that Resource (absent contractual considerations), or for New Import Bids below 0.75 times CONE, the opportunity cost or another reasonable economic measure, then the bid can set the Capacity Clearing Price. Otherwise, the New Capacity Bid or the New Import Bid (considered an "Out of Market Bid") shall be entered into the FCA pursuant to the Alternative Price Rule of Part III.I below.
3. If an RFP from the ISO covers any part of capacity costs, that capacity will be subject to the Alternative Price Rule.

I. **Alternative Price Rule.** If system-wide or in any import-constrained Capacity Zone: (a) new capacity is needed in the relevant Commitment Period; (b) the FCA is: (i) a Successful FCA or (ii) the FCA has Insufficient Competition pursuant to Part III.L.2 below but not Inadequate Supply pursuant to Part III.L.1; and (c) at the Capacity Clearing Price the purchases from the Out of Market Bids exceeds the required new entry, then the Capacity Clearing Price for that Capacity Zone shall be the lesser of: (1) the price at which the last New Capacity Bid withdrew from the FCA (excluding Out of Market Bids and bids in export-constrained Capacity Zones) minus $0.01, or (2) CONE; provided, however, that the price will be set to CONE in the event of Insufficient Competition if there are no withdrawn New Capacity Bids.

J. **Carry-forward rule.** If as a result of the rationing rule in Part III.D.6, the ISO purchases megawatts through an FCA in excess of the ICR for an

import-constrained zone, these extra megawatts shall create "carry-forward" accounts for the particular zones in which the corresponding physical assets are located.

Going into an FCA, if there are positive carry-forward balances, these megawatts shall be treated as Out of Market Bids subject to the Alternative Price Rule; except that if no new capacity is required in the zone, the resulting price shall not be greater than the Capacity Clearing Price in the FCA in which this carry-forward capacity originally cleared. Consequently, this rule shall apply even if the subsequent year's FCA was not competitive; provided that the earlier FCA (which set the Capacity Clearing Price for these carry-forward megawatts) was competitive. The carry-forward provision can apply to any import-constrained zone.

K. Bids Rejected for Reliability Reasons. A capacity Resource having a Permanent De-list Bid, De-list Bid, or Export Bid that is rejected for reliability reasons shall be paid a just and reasonable price (as determined by FERC) from the beginning of the Commitment Period and, for Permanent De-list Bids, for each subsequent Commitment Period (unless the reliability concern is addressed before the start of the Commitment Period) until it can be released to de-list. In such cases, the ISO shall attempt to procure replacement capacity at each FCA and annual reconfiguration auctions in order to release the capacity Resource to de-list. Payments to such Resources shall continue only until the reliability concern is addressed (through procurement of replacement capacity or other means, such as a transmission enhancement).

L. **Inadequate Supply and Insufficient Competition.** In the case of either Inadequate Supply or Insufficient Competition, both of which are defined below, the FCA shall still be used to the extent possible; that is, the remedy for Inadequate Supply or Insufficient Competition shall be limited to the Capacity Zones having Inadequate Supply or Insufficient Competition. In the event of FCA failure, the ISO shall try to identify the cause of the failure, and then take appropriate corrective action for future FCAs.

1. **Inadequate Supply.**

   a. **In a Capacity Zone.** A FCA will be considered to have Inadequate Supply in a Capacity Zone if at the Starting Price the amount of New Capacity (including imports) bid in the Capacity Zone is less than the amount of new capacity required in that Capacity Zone. In such an event, Existing Capacity in that Capacity Zone shall be paid 1.1 times CONE, New Capacity in that Capacity Zone shall be paid the Starting Price, and the deficiency shall be made up in subsequent reconfiguration auctions. Inadequate Supply in one or more Capacity Zones shall not affect the FCAs for Capacity Zones having adequate supply.

   b. **System-wide.** If the system-wide ICR cannot be satisfied at the Starting Price, then Existing Capacity shall be paid 1.1 times CONE, New Capacity will be paid the Starting Price, and the deficiency shall be made up in subsequent reconfiguration auctions. System-wide Inadequate Supply will not affect the FCAs for Capacity Zones

having adequate supply, except that, in those Capacity Zones having adequate supply, New Capacity shall be paid the Capacity Clearing Price, and Existing Capacity will be paid the lower of (1) the Capacity Clearing Price, or (2) 1.1 times CONE. If there is inadequate capacity system-wide but sufficient competition in an export-constrained Capacity Zone, the ISO shall hold the FCA for the export-constrained Capacity Zone, and in that case the price in the Rest-of-Pool Capacity Zone shall be the higher of 1.1 times CONE or the price in the export-constrained Capacity Zone.

2. **Insufficient Competition.** The FCA shall be considered to have Insufficient Competition system-wide or in any Capacity Zone if the following two circumstances are both satisfied:
   a. the amount of Existing Capacity is less than the ICR or the Local Sourcing Requirement as applicable; and
   b. at the Starting Price, (1) less than 300 MW of New Capacity (to be reconsidered in the case of import-constrained Capacity Zones with a total requirement of less than 5000 MW) is bid; (2) the amount of New Capacity bid is more than the amount of new capacity required but less than twice the amount of new capacity required; or (3) any Market Participant's New Capacity or New Import Capacity is pivotal unless such capacity is an Out of Market Bid. A Market Participant shall be considered pivotal if, at the Starting Price, some of that Market

Participant's potential New Capacity is required to satisfy the ICR.

If the FCA has Insufficient Competition, New Capacity shall be paid the Capacity Clearing Price, and Existing Capacity shall be paid the lower of (1) the Capacity Clearing Price, or (2) 1.1 times CONE. For the purposes of determining whether there is Insufficient Competition, New Capacity shall not include Import Capacity.

M. Reconfiguration Auctions. The ISO shall conduct annual reconfiguration auctions and monthly reconfiguration auctions. Participation in reconfiguration auctions is voluntary.

1. **Product bought and sold.** Reconfiguration auctions allow: (i) the ISO to purchase capacity requirements deferred from the FCA because of Inadequate Supply or incomplete replacement of Permanent De-List or De-List Bids; (ii) the ISO to buy additional capacity if the ICR has increased; (iii) the ISO to release capacity if the ICR has decreased; and (iv) physical Resources to trade their capacity commitments. Capacity clearing in the reconfiguration auctions shall be entitled to receive capacity payments for the period sold in the reconfiguration auctions.
2. **Qualification.** Supply offers in the annual reconfiguration auctions must submit qualification materials through the same process as the FCA. Demand bids must be filed with the ISO prior to the reconfiguration auction, specifying a maximum price, quantity, and the capacity Resource seeking to de-list (in part or in full). Offers and bids shall not be subject to mitiga-

tion. However, the performance of the market shall be subject to the review of the Market Monitor.

3. **Rationing Rule.** All supply offers and demand bids shall be subject to rationing.

4. **ISO Demand Bids and Supply Offers.** The ISO may offer to buy capacity as described in Part III.M.1 above. If the ISO seeks to buy capacity under clause (i) of that Part and also sell for the same Commitment Period capacity under clause (iii), only the net quantity shall be satisfied or released in a reconfiguration auction. The ISO shall offer to buy or sell the full amount of any deficit or surplus, respectively, from the then-current forecast of ICR in every subsequent reconfiguration auction, except as provided below. The ISO's demand bids shall be entered into the reconfiguration auction at a price of 2 times CONE. At prices above 0.75 times CONE, the ISO shall release all surplus capacity. Its sell offers shall follow a linear quantity rule that distributes the capacity for release between prices of 0.75 times CONE and 0.25 times CONE so that, if the price in a reconfiguration auction is below 0.25 times CONE, the ISO releases no surplus capacity.

5. **Locational Characteristics.** For any Commitment Period, capacity within any Capacity Zone that was in effect in the FCA, and for which there was price separation, shall be auctioned as distinct products in each subsequent reconfiguration auction for that period. Conversely, reconfiguration auctions shall not model any Capacity Zone that did not experience price separation in the primary FCA for that Commitment Period.

6. **Annual Auctions.** Annual reconfiguration auctions allow trading of whole-year commitments. Shortly after the FCA for year Y, the ISO shall conduct the annual reconfiguration auctions for year (Y – 1), then for year (Y – 2), and then for year (Y – 3), which is the "prompt" year. Each annual reconfiguration auction shall be a static double auction to clear offers to buy and sell. (A static double auction is a uniform-price auction in which sellers submit offers and buyers submit bids simultaneously. The clearing price is determined by the balance of supply and demand. All sell offers that clear are paid the clearing price, and all buy bids that clear pay the clearing price.) If there are no supply offers or if there are no demand bids for a particular product, no reconfiguration auction is held for that product. If the quantity of unfilled Permanent De-list Bids and De-list Bids or the amount of unmet ICR is sufficiently large, the ISO may also accelerate the next annual reconfiguration auction by six months.

7. **Monthly and Seasonal Auctions.** Beginning with the first month of the first Commitment Period cleared under the FCA, the ISO shall conduct reconfiguration auctions prior to each month for commitments during that month. Like the annual reconfiguration auctions, the monthly reconfiguration auctions shall be static double auctions. If there are no supply offers or if there are no demand bids for a particular product, no monthly reconfiguration auction will be held for that product.

   In addition to the monthly reconfiguration auctions described in the preceding paragraph,

the ISO will conduct reconfiguration auctions prior to the months of June and October for a "seasonal strip" product to trade whole-season commitments. The seasonal strip reconfiguration auction conducted prior to June will be for commitments covering the whole Summer Period of June through September, and the seasonal strip reconfiguration auction conducted prior to October will be for commitments covering the whole Winter Period of October through May. The seasonal strip reconfiguration auction for the Summer Period shall be conducted prior to the monthly reconfiguration auction for June, and the seasonal strip reconfiguration auction for the Winter Period shall be conducted prior to the monthly reconfiguration auction for October. Resources offering into monthly reconfiguration auctions may offer up to their capacity rating for that season or month, respectively.

8. **Availability Penalties.**

   a. Availability penalties shall be calculated based on the Capacity Clearing Price in the FCA for the relevant Commitment Period, except for any Resource under a multi-year Commitment Period, in which case the penalties for such Resource shall be set according to multi-year Capacity Clearing Price applicable to the Resource for the particular Commitment Period.

   b. **Penalty Caps.**

      i. **Obligations covered bilaterally.** If a capacity Resource owner covers its capacity obligation for part of the year through a bilateral transaction, the

availability penalty caps described in Part V.C.2.b and V.C.2.c shall apply to the sequence of Resources as though they were a single resource. It shall be the responsibility of the contracting parties to allocate the benefit of these caps among themselves.

ii. **Obligations covered through annual reconfiguration auctions.** If a capacity Resource owner sells its capacity obligation in an annual reconfiguration auction, the purchaser is subject to the same availability penalties and penalty caps that apply to a capacity Resource sold in the FCA for the relevant Commitment Period.

iii. **Obligations covered through Capacity seasonal or monthly reconfiguration auctions.** A capacity Resource that acquires a seasonal capacity obligation through a seasonal reconfiguration auction, or a one-month capacity obligation through a monthly reconfiguration auction cannot be charged availability penalties in excess of 2.5 times its monthly FCA Payment for any month in that Commitment Period, consistent with Part V.C.2.b. No capacity Resource on the system can be charged availability penalties in excess of its annual FCA Payment for that Commitment Period. If a capacity Resource is de-listed, in part or in full, for part of the year, the annual cap on availability penalties is not prorated,

except to the extent that the capacity obligation was transferred bilaterally as described in subpart (i) above.

N. **Interaction with Locational Forward Reserves Markets.** The Locational Forward Reserves Market ("LFRM") jointly filed by the ISO and NEPOOL in Docket No. ER06-613-000 shall not be changed by the Settlement Agreement. Parties retain their rights to address LFRM in proceedings before the FERC and retain their rights to address the interaction between the LFRM and the Forward Capacity Market in the stakeholder process that provides for consultation with state utility regulatory agencies and in proceedings before the FERC. The Parties agree to work to identify in the appropriate Market Rules how the LFRM and capacity markets will function together efficiently in the long run.

O. **Self-Supply Option.** As provided in Part II.F above, the Forward Capacity Market shall include a "self supply option," pursuant to which a LSE may designate as its FCA Resources Self-Supplied Capacity Resources that it owns or to which it has contractual rights. The amount of MWs of Resources so designated for a Capacity Zone may not exceed the LSE's projected ICR obligation for the applicable Commitment Period in that Capacity Zone.

P. **Bilateral Contracting.** Bilateral contracts shall be allowed up to the applicable Seasonal Claimed Capability of the Resource for that applicable month. Any Resource accepting a capacity obligation pursuant to a bilateral contract shall be subject to the qualification requirements of Existing or New Capacity, as applicable.

IV. Agreements Regarding Rights and Obligations.

A. Listed Capacity. Listed Capacity shall have the following rights and obligations, effective the first Commitment Period of the Forward Capacity Market.

1. The listed portions of Resources must offer into both the Day-Ahead and Real-Time Energy Markets whenever available. The current Day-Ahead Energy Market obligations of Intermittent and demand Resources are not changed by this Settlement Agreement.
2. Day-Ahead Energy Market offers from capacity Resources must either:
   a. have a sum of start time plus minimum run time plus minimum down time that is less than or equal to 72 hours; or,
   b. for Resources that due to physical design limits cannot meet the offer requirement in subpart IV.A.2.a., be bid in at zero in Day-Ahead or Self Scheduled on.
   c. Capacity Resources that meet the offer requirement in subpart IV.A.2.a. may also Self Schedule.
3. For each day, Day Ahead and Real Time offers for the listed portion of a Resource must reflect the then-known unit-specific operating characteristics (taking into account, among other things, the physical design characteristics of the unit) consistent with good utility practice. Capacity Resources must re-declare to the ISO any changes to the offer parameters that occur in real time to reflect the known capability of the Resource.

4. Appendix B of Market Rule 1 will be modified as necessary and consistent with Part VIII of this Settlement Agreement to apply to listed portions of Resources during the Transition Period. Following the Transition Period, Appendix B will be revised to reflect the following economic penalties, which shall be in addition to any availability penalties pursuant to Part V.C.2 resulting from a failure to perform during a Shortage Event:
    a. Intentional violations of Part IV.A.3 shall be subject to the following penalty structure:
        i. For the first violation: warning.
        ii. For the second violation: up to daily FCA Payment ($/kW-day) for affected (kW), capped at $150,000.
        iii. For the third violation: up to 2 times daily FCA Payment ($/kW-day) for affected (kW), capped at $300,000.
        iv. For the fourth violation: up to 4 times daily FCA Payment ($/kW-day) for affected (kW), capped at $600,000.
        v. For any violations after the fourth violation: all remedies available under the FPA, without limitation.
    b. For purposes of establishing penalties pursuant to Part IV.A.4.a above, violations must occur in a 90 day period in order to be cumulative. In order to constitute a violation following a warning or prior violation, the violations must (i) be similar in nature and relate to either the same unit or a unit with similar operating characteristics that

is owned directly or indirectly by the same entity and has its bid parameters submitted by the same entity, and is alleged to have committed the same violation of Part IV.A.3; and (ii) the entity subject to potential penalty must have had an opportunity to confer with the ISO following receipt of the notice of the warning or prior violation as described in Part IV.A.4.d below.

c. If multiple units with similar operating characteristics that are owned directly or indirectly by the same entity and have their bid parameters submitted by the same entity are alleged to have committed the same violation of Part IV.A.3 during the same bidding days, the violation shall be counted as a single violation for the similar units.

d. Assessment of Penalties for violations shall be subject to the following general due process rights:

   i. Timely Notice. The ISO must give a warning or notice within 10 days of the observed behavior (in order to ensure that the generator has relevant information regarding the rationale behind the bid).

   ii. Opportunity to Confer with the ISO. A generator must be given the opportunity to respond within 3 business days of the warning/notice with its rationale supporting its bid parameter(s), including relevant documentation, if any. If the ISO concludes that the observed behavior was not an intentional failure

to bid in accordance with Section IV.A.3, the warning or notice will not count for purposes of applying a penalty.

iii. Imposition of Penalty. A Resource shall have the ability within 5 business days after conferring with the ISO pursuant to Part IV.A.4.d.ii to petition the FERC Office of Market Oversight and Investigations ("OMOI") to address any disagreements with the ISO as to whether the particular behavior constituted an intentional failure to bid in accordance with Part IV.A.3. If OMOI concludes that the behavior that is the subject of the warning is not an intentional failure to bid in accordance with Section IV.A.3, the warning will not count for purposes of applying a penalty. The issuance of the warning by the ISO and the petition to the OMOI shall be conducted on a confidential basis without notice to any other party; provided however, that the issuance of a warning that is not petitioned to the OMOI may be made public by the ISO. Any penalties imposed pursuant to this section shall be filed publicly at FERC and shall be imposed only by FERC order.

5. Economic outages are not permitted for capacity Resources. If due to extraordinary fuel prices, a Market Participant cannot submit a bid which would recover its full operational cost, it may then submit a Supply Offer in the

Day-Ahead Energy Market or in the Real Time Energy Market at the Offer Cap (or highest level allowed by the software) and contemporaneously advise the ISO that the Supply Offer would have been equal to or greater than the Offer Cap but for the Supply Offer Cap specified in Market Rule 1, Section III.1.10.1A(d)(viii) (the "Offer Cap") and provide the ISO with a statement of what the Supply Offer would have been but for the Offer Cap (the "Offer"). If the capacity Resource is subsequently dispatched for the period covered by the Offer, the Market Participant shall be paid its Offer for each MWh of Energy produced from the applicable generating Resource through the payment of the Locational Marginal Price and, appropriate Net Commitment Period Compensation ("NCPC") Credits, provided that such payment shall not exceed the capacity Resource's fuel costs, including commodity cost, transportation applicable to transporting cost related to the generation in the bid, and imbalance charges or other penalties applicable to such generation. NCPC Credits and Charges will be allocated in accordance with Appendix F of Market Rule 1.

6. A Resource that transfers its capacity market obligations to another Resource either through a reconfiguration auction or a bilateral contract pursuant to Part III.P and as applicable subject to Part III.M.8 will be relieved of its capacity Resource obligations and shall be delisted pursuant to the de-listing process to be developed in the Market Rules and the contracting entity will assume those obligations.

B. De-listed Capacity. De-listed Capacity shall have the following rights and obligations, effective the first Commitment Period of the Forward Capacity Market.

1. Rules with respect to De-listed units, including Permanent De-listed units and Export Capacity units, shall apply only with respect to the De-listed portion of a unit, and obligations with respect to listed portions shall be unaffected.
2. All or a portion of a capacity Resource that does not clear in a FCA, and any portion of such Resource for which a Permanent De-list Bid, De-list Bid, or Export Capacity (as an accepted Export Bid or bilaterally sold pursuant to Part III.P) has been accepted, was de-listed pursuant to Part III.D, or has transferred its obligation pursuant to Part IV.A.6 is not otherwise committed to provide capacity pursuant to a bilateral contract or reconfiguration auction ("De-listed Capacity"), is not required to offer the De-listed Capacity into the Day-Ahead or Real-Time Energy Market or honor the ISO's requests to reschedule maintenance during the Commitment Period for that FCA.
3. De-listed Capacity may be offered into the Day-Ahead Energy Market and, if accepted, shall be subject to the same rules as all other Resources in that Market (including the obligation to follow the ISO dispatch instructions). Such De-listed Capacity may be self-scheduled for portions of units not accepted into the Day-Ahead Energy Market.
4. De-listed Capacity not offered into the Day-Ahead Energy Market must Self-Schedule in order to participate in the Real-Time Energy

Market. Any De-listed Capacity, including any portion of a de-listed unit, that is offered into the Day-Ahead Energy Market but accepted neither in whole nor in part must also Self-Schedule to participate in the Real-Time Energy Market. The ISO may request that such a Resource provide Energy, but the Resource shall not be obligated to come on line and shall not suffer any performance or availability penalties if it does not come on line.

C. **Self-Supplied FCA Resource.** A Self-Supplied FCA Resource shall be subject to the same "Rights and Obligations" as any other capacity Resource that is accepted in the FCA.

V. Agreements Regarding Payments and Charges.

A. **Capacity Clearing Prices.** Capacity Clearing Prices shall be determined for each Capacity Zone in the FCA. Each capacity Resource clearing in the FCA, or otherwise covered by a multi-year commitment, but not a Self-Supplied FCA Resource, shall be entitled to monthly payments based on the product of its MWs of capacity cleared in the relevant FCA and the Capacity Clearing Price in the appropriate location in the New England Control Area (the "FCA Payment"); provided that FCA Payments to New Capacity shall be limited to the capability demonstrated as contemplated by either Part III.D.1 or Part III.D.4.a, as necessary. The FCA Payment shall be decreased for PER pursuant to Part V.B. below and adjusted for availability penalties or credits pursuant to Part V.C. below.

1. **Capacity with a one-year Commitment Period.** Capacity with a one-year Commitment Period (that is, Existing Capacity, Import Capa-

city and New Capacity electing a one-year Commitment Period) shall receive monthly capacity payments based on the FCA Capacity Clearing Price for the one-year Commitment Period.

2. **Capacity with a multi-year Commitment Period.** New Capacity with a multi-year Commitment Period (that is, New Capacity electing a Commitment Period of anywhere from two to five years, in one-year increments) shall receive monthly capacity payments based on the FCA Capacity Clearing Price that is associated with the first year of the Commitment Period for each of the years of its Commitment Period. After the first year of the Commitment Period, the price paid to that New Capacity shall be adjusted to account for inflation using an agreed-upon index to be determined in the Market Rules. (In other words, the FCA Capacity Clearing Price that applies in the first year of the Commitment Period for that New Capacity shall also apply, adjusted for inflation, in each year of the remainder of the multi-year Commitment Period.)

3. **Capacity in the Reconfiguration Auction.** Capacity clearing in a reconfiguration auction shall receive monthly capacity payments based on the reconfiguration auction clearing price for the relevant portion of the Commitment Period.

B. **Peak Energy Rents ("PER").** Payments to capacity Resources shall be decreased by PER as provided in this Section V.B.

1. **Hourly PER Calculations.**

   a. For hours with a positive difference between the energy price and a "strike price" equal to the deemed incremental cost of a marginal "proxy unit," the ISO shall compute a PER for each hour ("Hourly PER") equal to this positive difference in accordance with the following formula, which includes scaling adjustments as described in Part V.B.1.c and V.B.1.d.iv below:

      Hourly PER = [(LMP – strike price) * (scaling factor "50/50")] * [the Availability Factor (0.95)]

      This Hourly PER shall be summed for the month to determine the total PER for the month ("Monthly PER"). The ISO shall then calculate the average Monthly PER earned by the proxy unit for the most recent 12 months. This Monthly PER shall be deducted from the payment due to the listed portion of each capacity Resource in the month.

   b. The PER calculation shall utilize hourly integrated Real-Time LMPs.

      i. If there is zonal price separation in the FCA, PER shall be computed based on Real-Time LMPs for each Capacity Zone (using the Real-Time Hub price for the Rest-of-Pool Zone).

      ii. If there is no price separation in the FCA, PER shall be computed based on the Real-Time Hub price.

c. The PER calculation shall be scaled hourly based on the ratio of actual hourly integrated system load and the "50/50" predicted peak system load used in establishing ICR, capped at an hourly ratio of 1.0.

d. PER "proxy unit" characteristics shall be as follows:

   i. The PER "proxy unit" shall be indexed to the marginal fuel, with additional detail to define how to determine the marginal fuel to be reflected in a Market Rule;

   ii. The PER "proxy unit" shall be assumed to have no start-up, ramp rate or minimum run time constraints;

   iii. For at least the first Commitment Period, the PER "proxy unit" shall be deemed to have a 22,000 BTU/kWh heat rate. This assumption shall be periodically reviewed after the first Commitment Period by the ISO to ensure that the heat rate continues to reflect a level slightly higher than the marginal generating unit in the region that would be dispatched as the system enters a scarcity condition. Any changes to the heat rate of the PER "proxy unit" shall be considered in the stakeholder process in consultation with the state utility regulatory agencies, shall be filed pursuant to Section 205 of th[e] FPA, and shall be applied prospectively only to future FCAs.

iv. The PER "proxy unit" availability is deemed to be 95%. The PER shall be scaled by this availability factor.

2. **Monthly PER Application.**
   a. FCA Payment shall be reduced by a 12-month rolling average PER adjustment calculated prior to the prompt month.
   b. The rolling 12-month average PER calculations for Capacity Zones that become either constrained or unconstrained (import or export), shall include a locationally determined PER in each month that the constraint binds in the FCA.
   c. PER tracks energy revenues and therefore shall be deducted from capacity payments independently of availability adjustments.
   d. FCA Payment minus PER cannot be negative for any month.
3. **Self-Supplied FCA Resources.** Self-Supplied FCA Resources shall not pay a PER adjustment. LSEs satisfying their ICR obligations by a Self-Supplied FCA Resource shall not receive a credit for any PER payment for their ICR obligations so satisfied.

C. **Availability Metric:** Modified Shortage Hours. Payments to capacity Resources shall be adjusted to reflect the performance of those Resources during Shortage Events as provided in this Part V.C.

1. **Definition of "Shortage Events":**
   a. System-wide Reserve Constraint Penalty Factors ("RCPFs") shall trigger a Shortage Event.
   b. A Shortage Event may also be triggered solely in an import-constrained region if

there is price separation for the applicable Capacity Zone in the FCA and an OP4 Action 6, OP4 Action 12, OP4 Action 13, or OP7 event in that Capacity Zone has been declared solely in the import-constrained zone, where such declaration is based on adequacy (versus security).

c. An export-constrained region shall be exempt from a Shortage Event if there is price separation for the applicable Capacity Zone in the FCA and an OP4 Action 6, OP4 Action 11, OP4 Action 12, OP4 Action 13, or OP7 event has been declared for the Rest-of-Pool Capacity Zone but not for that export-constrained Capacity Zone.

d. A discrete Shortage Event is defined as any contiguous period of RCPF activation with a minimum duration of 30 minutes, or, in an import or export-constrained region, an OP4 action or OP7 event identified in Parts V.C.1.b and V.C.1.c above with a minimum duration of 30 minutes. Such activations, actions and events must be separated by at least 2.5 hours to be considered discrete Shortage Events. There may be a maximum of two Shortage Events per day.

2. **Availability Penalties.**

a. For Resources that are unavailable during a Shortage Event:

i. Penalties shall be determined and assessed on a Resource-specific basis.

ii. The penalty per Resource for each event shall be 5% of its FCA Payment

for that year, subject to sub-Parts V.C.2.a.iii. through V.C.2.a.v. below.

iii. The penalty for the portion of the Shortage Event during which the Resource was unavailable shall be prorated based on the number of hours (or fractions of hours) that the Resource was available in such Event.

iv. The penalty shall be further prorated based on the hourly ratio of available MW, as determined below, to the Summer Seasonal Claimed Capability of the unit (or amount sold in the FCA if less).

v. For discrete Shortage Events that exceed five hours, the penalty shall be increased by 1% per hour.

vi. In no case shall the total penalties for all Shortage Events in an operating day exceed 10% of the Resources' FCA Payment for that year.

b. The total of a Resource's penalties arising from unavailability during a calendar month cannot exceed two and one-half times the total FCA Payment for that calendar month. The total of a Resource's penalties arising from unavailability due to a single outage of four days or less but spanning two calendar months cannot exceed two and one-half times the average of the total FCA payments for both months.

c. The total of a Resource's annual penalties cannot exceed its total FCA Payment less PER adjustments for that year.

3. **Availability Credits.** On a monthly basis, penalties received from unavailable Resources shall be redistributed to listed Resources that were available in the respective hour(s) using the following distribution method: For each Shortage Event in a month, the penalties assessed for that event will be credited to those Resources that were available, in whole or in part, during that event, pro-rata by hourly available MW in the relevant Capacity Zone(s).
4. **Definition of "Available."** A Resource shall be deemed available: (i) if it is on line and following the ISO dispatch instructions, to the extent of its available EcoMax; or (ii) if it has a notification plus start-up time of 30 minutes or less, to the extent of its available EcoMax; or (iii) if it meets the requirements of any of the following sub-parts V.C.4.a. through V.C.4.d:
    a. A Resource with notification plus start-up times less than or equal to 12 hours that was competitively bid but was not committed by the ISO because it was not needed to satisfy the market's anticipated energy and reserve needs and is consequently unavailable within 30 minutes, provided the Resource shall not be considered available if it fails to come on line in accordance with its verified unit characteristics when called by the ISO either in its Resource Adequacy Assessment process or otherwise prior to or during the delivery day. For the duration of the first five annual FCA Commitment Periods, existing Resources with notification plus start-up times greater than 12 hours, as of the date of the Settlement

Agreement, will be subject to a notification and start-up time criteria of 16 hours rather than 12 hours (subject to Part IV.A.3. above regarding offer parameters). Thereafter, all existing and new Resources will be subject to the 12-hour criterion.

b. A Resource not committed due to a transmission outage, or derate in New England other than an outage or derate of such transmission equipment (i) controlled by the internal Resource; or (ii) constituting a radial lead to a[n] internal Resource (other than radial leads to Wyman 4 and Stony Brook). In addition, a Resource in a Capacity Zone that was export-constrained in the FCA shall not be subject to a Shortage Event in the circumstances described in Part V.C.1.c. Unless otherwise provided for in a separate settlement provision, Maine Independence Station shall not be deemed to be unavailable for capacity purposes when derated or not committed because of a constraint on the Orrington South, Surowiec South or Maine – New Hampshire interfaces.

c. Import Capacity that has been properly offered in the Day-Ahead Energy Market that cannot make Real-Time deliveries because the relevant transmission element is fully loaded in Real Time;

d. A Resource that is on maintenance approved in the ISO's annual maintenance scheduling process, provided that:

i. The Resource has not scheduled such maintenance in December through January or June through mid-September, unless the ISO requests the Resource to schedule its annual maintenance during one of those periods; and

ii. The Resource has not exceeded the maximum allowable days of annual maintenance as established by the ISO standards, which standards shall be subject to the stakeholder process in consultation with state utility regulatory agencies and consistent with good utility practice.

5. If a capacity Resource temporarily does not meet the requirements of either subparts IV.A.2.a. or IV.A.2.b. above, the Resource must declare itself to be unavailable.

6. A capacity supplier can supplement the shortage hour availability performance of its unavailable "listed" Resource in a Shortage Event by purchase of a Resource that is not listed, provided that the substitute Resource accepts all of the associated capacity obligations of a "listed" Resource.

7. **Poorly Performing Units.** The availability score of a Resource in a given year shall be calculated as the number of hours of availability during Shortage Events divided by the total number of Shortage Event hours during a year. In the event that there are no Shortage Event hours during a year, the availability score is 100 percent. Prior to qualifying a Resource to participate in the FCA, the ISO shall determine whether a Resource meets the fol-

lowing two criteria: (a) if, in any four year period, a Resource received three availability scores of less than or equal to 40 percent; and (b) the Resource has failed to be available during at least ten Shortage Events during that same four-year period. If both of these criteria are met, the Resource shall be considered a Poorly Performing Unit and shall not be eligible to participate in the FCA or be designated as a capacity Resource until (as a non-capacity Resource) it either achieves an availability score of 60 percent or higher in three consecutive years or has demonstrated to the satisfaction of the ISO that the source of the inadequate availability score has been remedied. For the purposes of determining whether a Resource is a poorly performing unit, its availability score while it is de-listed shall not be considered. For the purposes of returning from poorly performing status, the ISO, at the request of the Resource owner, may consider performance while de-listed. The ability to request consideration of performance while delisted in support of returning from poor performing status shall not be construed as to imply an ability to choose non-consecutive years for evaluation.

8. **Intermittent Resources and Demand Resources.** Intermittent Resources and demand Resources shall be exempt from the availability penalties and credits of this Part V.C.

9. **Self-Supplied FCA Resources.** Self-Supplied FCA Resources are subject to the same availability penalties and credits as other Resources participating in the FCA. If a Self-Supplied FCA Resource is unavailable during a Short-

age Event, the LSE designating that Resource shall be responsible for paying the associated availability penalty based upon the Capacity Clearing Price for that Commitment Period. Self-Supplied FCA Resources shall be eligible to receive their pro-rata share of availability penalties paid by other capacity Resources.

VI. Agreements Regarding External Resources. Market Rules, operating procedures and manuals shall be changed to allow External Resources to participate in the Forward Capacity Market and Transition Period on a basis comparable to internal generation Resources. Among the changes that are required are that the timing for Real Time contract submittals be modified to allow them to be made after the Day Ahead Energy Market closes and as soon as one hour before an operating hour in order to allow for the purchase of required transmission.

VII. Agreements Regarding Gas Availability. For the winter season of the first Commitment Period under the FCA and for each subsequent winter season, the following provisions shall apply:

A. **Adjustment of Deadlines.** The normal times for the Day-Ahead Energy Market bid and offer deadlines, the posting of Day-Ahead Energy Market results and the initial Resource Adequacy Assessment ("RAA") process shall be rolled back to earlier time periods during the peak winter months of December, January and February such that the results of the Day-Ahead Energy Market and initial RAA are available by a target completion time of 10:30 a.m. of the day prior to the electric Operating Day. The Day-Ahead Energy Market will normally be cleared and posted within

four hours of the deadline for submitting Day-Ahead Energy Market bids and offers. The initial RAA will be run after the posting of the Day-Ahead Energy Market results with a scheduled completion of [ ] 10:30 a.m. The start of the Re-offer period shall be open immediately after the initial RAA run.

B. Procurement of Supplement Reserves and Payments. For days that the ISO forecasts a Cold Weather Warning or Cold Weather Event (as currently described in Appendix H of Market Rule 1) for the next Operating Day, the ISO shall include in the initial RAA process the procurement of an additional 1000 MW per hour of Supplemental Reserves for peak load periods of the day from gas fired resources that are required to rely exclusively on gas for their operations that Operating Day and not already participating in the Forward Reserve Market. At the completion of the initial RAA, the ISO shall notify Resources of the expected energy schedule incremental to the Day-Ahead Energy Market results, if any, plus the applicable reserve MWHs, for the respective unit. For such Cold Weather operating conditions, the outcome of this initial RAA shall be financially binding for the incremental gas fired generation (i.e., gas-fired generation beyond that gas-fired generation scheduled in the Day-Ahead Energy Market) scheduled in the initial RAA. In addition, the MWHs of Supplemental Reserves scheduled from gas-fired generation scheduled for these Cold Weather Warning periods in accordance with the understandings in this part will be compensated pursuant to the formula below (or similar method) for resale of gas reserved, purchased and nominated for such Supplemental Reserves. The

natural gas volume (Scheduled Volume) obtained by Resources eligible for such compensation shall be based upon the particulars of the noticed schedule: (the total hours of requested service, total MWs per hour and the unit's applicable heat rate). If the ISO does not dispatch energy from the scheduled Supplemental Reserves to the full extent committed pursuant to this understanding, then those generators will be compensated for the portion of the Supplemental Reserves not dispatched for energy in accordance with the following formula:

(Daily Gas Index for Gas Day scheduled flow date – Daily Gas Index for first Gas Day for which flow orders have been removed to allow the sale of the gas that was held for reserve service) × (Undispatched reserved gas volume).

The Daily Gas Index applicable to each gas-fired Resource shall be based on the index used by the Market Monitor for establishing Reference Levels for that Resource under Section III.A.5.6.1(b)(i) of Appendix A of Market Rule 1. The ISO shall establish a methodology for determining applicable prices from the appropriate index that are reasonably designed to reflect the difference between (1) prices on the scheduled flow date and (2) prices for the resale of gas scheduled to meet that Resource's binding obligations but not burned to generate electricity at the location of the affected Resource during Cold Weather Warnings and Cold Weather Events. The ISO shall communicate that methodology for determining prices from the applicable index to the Governance Participants for consideration pursuant to the stake-

holder process for considering Market Rules and changes, and shall file the methodology with FERC pursuant to Section 205 of the FPA.

C. **Confirmations.** For days that the ISO forecasts Cold Weather Warnings and Cold Weather Events, sufficiently in advance of pipeline gas nominating deadlines, all gas-fired Resources shall confirm to the ISO that they will nominate sufficient fuel to be able to deliver the energy and Supplemental Reserves scheduled in the Day-Ahead Energy Market and initial RAA results respectively. Following the Initial RAA but no later than 6:00 p.m. of the day preceding the electric Operating Day, each gas-fired Resource shall provide to the ISO confirmation and evidence of gas volume nomination of sufficient fuel to be able to deliver the energy scheduled for such Resource in the Day-Ahead Energy Market and the Supplemental Reserves that were identified for that Resource in the initial RAA.

VIII. Agreements Regarding Transition Period.

A. The current UCAP products shall be retained for the period commencing on December 1, 2006 and ending on May 30, 2010 (the "Transition Period') as provided for in Part VIII.I. Payments will be made to UCAP entitlement holders, and made by UCAP obligation holders including wholesale standard offer suppliers in Rhode Island as under the current Market Rules and tariffs; it being understood that the agreement of wholesale standard offer suppliers in Rhode Island to make UCAP payments is contingent upon the agreement of the state of Rhode Island utility regulatory authorities to support the settlement.

B. All listed ICAP Resources shall receive the following fixed payments, based on their seasonal UCAP ratings:

December 1, 2006 to May 31, 2007	$3.05/kW-month
June 1, 2007 to May 31, 2008	$3.05/kW-month
June 1, 2008 to May 31, 2009	$3.75/kW-month
June 1, 2009 to May 31, 2010	$4.10/kW-month

These payments are fixed and shall not be adjusted for changes in UCAP quantity.

C. There shall be no PER adjustments to any of the above payments.

D. Availability shall be measured by a weighted EFORd approach, as follows:

Outage Period	**Weighting Factor**
Off-Peak Hour	0.0
On-Peak Hour	1.0
Seasonal Peak Hour	20.0
Shortage Hour	40.0

Outage Period definitions:

On-Peak	Hours – ending 8:00 a.m. through 11:00 p.m. on all non-NERC holiday weekdays.
Off-Peak	All hours that are not On-Peak hours.
Seasonal Peak	The 200 hours pertaining to the highest 100 hourly system loads during the Summer Period (for this purpose, June through September) and the highest 100 hourly system loads during the Winter Period

	(for this purpose, October through May).
Shortage Hour	Periods of system-wide OP4, Action 6 or 11 or OP7 implementation.

Weighting factor shall not be additive (i.e., a Shortage Hour does not have a weighting factor equal to 61). A Resource's availability factor for purposes of UCAP ratings (*i.e.*, UCAP settlement credit) in settlement shall be a rolling average of the unit's seasonal weighted EFORd, with seasons as defined in the Seasonal Peak provision above. In months in which the Resource is de-listed, the unweighted EFORd shall apply. Weighted EFORd shall be phased-in over the first two seasons of the Transition Period. For the first six calendar months of the Transition Period, corresponding to the remaining portion of the 2006/2007 winter season, the ISO will gather the data necessary to calculate weighted EFORd for this season. However, for payment purposes during this time, the availability score will be based on twelve-month rolling unweighted EFORd.

During the 2007 summer season, the availability score will be calculated as 50 percent weighted EFORd from the 2006/2007 Winter Period (i.e., October 2006 through May 2007) and 50 percent unweighted EFORd, calculated using six months of data prior to transition (i.e., April 2006 through September 2006). At the conclusion of the 2007 summer season, a weighted EFORd score shall be calculated for that season, and that score shall replace the unweighted EFORd score in the calculation above. For the remainder of the Transition Period, the weighted EFORd score of each Re-

source shall be updated coincident with each new winter and summer season, using the process described above.

The method for converting the ICRs in Section 1.4 of Manual 20 shall continue to be based on the EFORd determined under the current equal weighting of all hours.

If additional measures need to be taken by the ISO to protect reliability during the Transition Period, the ISO retains its right to make filings pursuant to Section 205 of the FPA as appropriate, subject to stakeholder process.

E. Unless otherwise agreed in a FERC-approved settlement, transition payments shall be netted against RMR payments. Transition payments shall be considered capacity payments for purposes of netting in the LFRM markets.

F. For the purpose of any RMR agreements that have provisions that terminate such RMR agreements upon the implementation or effectiveness of a locational ICAP mechanism, the Transition Period shall not be considered to be the implementation or effectiveness of a locational ICAP mechanism and the beginning of the first Commitment Period of the FCA shall be considered to be the implementation or effectiveness of a locational ICAP mechanism. Notwithstanding the foregoing, and absent an FERC-approved settlement, nothing herein prejudices the rights of any party to challenge, seek to terminate or support an RMR agreement on any other grounds or restrict any party's rights to seek, agree to or oppose any RMR modifications.

G. Suppliers shall be permitted to partially delist or export their units.

H. Commitment periods shall be seasonal, summer (May – October) and winter (November – April). For 2006, the Winter Commitment Period shall begin on December 1, 2006. Imports qualify with a minimum 2-month commitment (consecutive months in the same season). Exports do not receive payment.

I. 2010/2011 Commitment Period Special Pricing Rule. If the ISO conducts the first FCA in the first quarter of 2008 for the Commitment Period beginning June 1, 2010, and the FCA fails either the Inadequate Supply or Insufficient Competition test, then any New Capacity Resources selected in the FCA shall be paid the FCA starting price or FCA Capacity Clearing Price, as appropriate, in the 2010/2011 Commitment Period and Existing Capacity shall be paid the average of all Successful FCAs held prior to the 2010/2011 Commitment Period. If subsequent FCAs also fail, or if the 2010/2011 FCA cannot be held, all existing listed ICAP Resources in the 2010/2011 Commitment Period shall be paid $4.70 per kW-month in accordance with the provisions of this Part VIII.

J. Intermittent and Demand Resources.

1. **Intermittent Resources.** During the Transition Period, Intermittent Resources shall continue to receive the treatment for determining capacity and availability in effect under the current Market Rules, Tariffs and Manuals.

2. **Demand Resources.**

   a. Real Time Demand Response during the Transition Period shall remain as qualifying capacity Resources subject to Market Rule 1 Appendix E and the Load Response Manual. As such, the role of demand re-

sponse resources in the market will continue to evolve as Market Rule 1 Appendix E and the Load Response Manual are revised.

b. During the Transition Period, new (as of the Effective Date) demand side management installations (both energy efficiency and demand response, other than Real Time Demand Response) undertaken as part of merchant, utility, or state sponsored programs will be considered as qualified capacity and subject to the ISO review of the verification process. Details concerning how these programs qualify as capacity Resources will be reflected in the Market Rules.

K. Phase I/II HQ Interconnection. During the Transition Period, the total transfer limit of the HQ Phase I/II interconnection with Hydro-Quebec shall be fixed at 1800 MW for UCAP purposes, as set forth below. Except as set forth below in this subsection, the total MWs of HQICCs shall be fixed at 1200 MW March through November and zero MW December through February, shall receive payment in the non-zero months under Part VIII.B and I, and otherwise continue to receive the treatment for determining capacity and availability in effect under the Market Rules (Market Rule 1 Section III 8.3.2(a)(v)), Tariffs and Manuals as of March 6, 2006. The remaining 600 MW of transmission may be used for UCAP over the Phase I/II interconnection by any supplier that arranges for transmission over the interconnection without reductions in the HQICCs. UCAP above 600 MW may be transmitted only in those

months when the HQICCs are 1,200 MW and will result in reductions in HQICCs as provided for under current procedures. Only the remaining HQICCs will receive UCAP payments under Part VIII.B and I. UCAP delivered over the Phase I/II facilities shall receive payment under this Part VIII.B and I. Non-HQICC UCAP delivered over the Phase I/II facilities shall continue to receive the treatment for determining capacity and availability in effect under the Market Rules as they may be modified pursuant to Part VI of this agreement.

IX. Consideration of Expedited Treatment for Challenges to Certain ISO Determinations that Must Be Final Prior to the FCA. Not later than 90 calendar days prior to the conduct of each FCA, the ISO shall make an informational filing at the FERC in which the ISO shall identify the determinations listed below in Part IX.A through C and provide supporting documentation for each such determination. Interested entities will have 15 days thereafter to file comments on or challenges to the determinations in that informational filing. Unless the FERC issues an order to the contrary within 75 calendar days following that informational filing, such determinations contained in the filing shall be used by the ISO in the next FCA, and the Capacity Clearing Price derived through that FCA shall be subject to the finality provisions of Section 4.C. If the FERC does issue an order to the contrary, absent further direction from the FERC, the ISO shall use the revised determinations reflected in that order in the ensuing FCA, which shall be conducted no earlier than 15 days following that order. Once the ISO has used such a revised determination in the FCA in accor-

dance with the provisions of this Part IX, the Capacity Clearing Price derived through the applicable FCA shall be subject to the finality provisions of Section 4.C.

A. The ISO's determinations pursuant to Part III.A.

B. Resources that satisfy the qualifications in this Settlement Agreement and the Market Rules that address the terms of this Settlement Agreement to participate in an FCA or reconfiguration auction specifically.

C. Market Monitor conclusions concerning acceptability of Bids in any FCA.

ATTACHMENT 1-A

ATTACHMENT A

SETTLEMENT AGREEMENT RESOLVING ALL ISSUES

Definitions. This Attachment A consolidates, references and summarizes capitalized terms that are used in the Settlement Agreement. This Attachment is for convenience only and should not be considered a part [of] the Settlement Agreement itself. Except as specifically defined within the Settlement Agreement, the capitalized terms are from the ISO Transmission, Markets and Services Tariff or other operative documents, and the definitions below are to definitions as they now appear in those documents, and are subject to change from time to time pursuant to those documents.

"Alternative Price Rule" is defined in Section 11, Part III.I of the Settlement Agreement.

"Billing Policy" is Exhibit ID to Section 1 of the Tariff.

"Capacity Clearing Price" is the clearing price in the FCA for each Capacity Zone determined in accordance with Section 11, Part III.G of the Settlement Agreement and as more fully described in Section 11, Part III of the Settlement Agreement.

"Capacity Zone" is the geographic sub-region in the New England Control Area that is determined by the ISO in accordance with Section 11, Part III.A of the Settlement Agreement based on an identification of transmission limits that may bind in the FCA.

"Cold Weather Condition" is the existence of Effective Temperatures $\leq$ 0 degrees Fahrenheit (on peak hours) and Effective Heating Degree Days $\geq$ 65.

"Cold Weather Event" is a day when Cold Weather Conditions are forecast to exist and the ISO forecasts a system wide capacity deficiency requiring the implemen-

tation of OP-4 actions (i.e., the 7-day capacity margin forecast ≤ 0 MW for an Operating day).

"Cold Weather Warning" is a day when Cold Weather Conditions [are] forecast to exist and the ISO forecasts tight capacity conditions (i.e., the 7-day capacity margin forecast > 0 MW and < 1,000 MW).

"Commitment Period" is [ ] a period of either one year in duration (corresponding to the Power Year for which the FCA is held) or, for New Capacity, up to five years in duration (beginning with the Power Year for which the FCA is held), as described in more detail in Section 11, Part II of the Settlement Agreement.

"Conditional Approval Order" is a FERC order accepting or approving the Settlement Agreement conditioned on the modification of any of the terms of the Settlement Agreement.

"Cost of New Entry" or **"CONE"** is determined in accordance with Section 11, Part III.F of the Settlement Agreement.

"Day-Ahead" is the calendar day immediately preceding the Operating Day.

"Day-Ahead Energy Market" is the schedule of commitments for the purchase or sale of energy, payment of Congestion Costs, and payment for losses developed by the ISO as a result of the offers and specifications submitted in accordance with Section III.1.10 of Market Rule 1.

"De-list Bid" is a bid from Existing Capacity submitted in an FCA to be removed from the Forward Capacity Market, as described in more detail in Section 11, Part III.D.5 of the Settlement Agreement.

"De-listed Capacity" is all or a portion of a Capacity Resource[ ] that does not clear in a FCA, and any portion of such Resource for which a Permanent De-list Bid or De-list Bid has been accepted or has transferred its obli-

gation pursuant to Section II, Part IV.A.6 of the Settlement Agreement is not otherwise committed to provide capacity pursuant to a bilateral contract or reconfiguration auction.

"Deposit" is the financial assurance provided by New Capacity in order to submit a bid in a FCA for which it has been qualified pursuant to Section 11, Part II.B.3 of the Settlement Agreement.

"Economic Minimum Limit" or **"EcoMin"** is the maximum of the following values: (i) the minimum generation amount, in MWs, that a generating unit can deliver for a limited period of time without exceeding specified limits of equipment stability and operating permits; (ii) a level supported by environmental and/or operating permit restrictions; or (iii) a level that addresses any significant economic penalties associated with operating at lower levels that can not be adequately represented by three-part bidding. In no event shall the Economic Minimum Limit submitted as part of a generating unit's Offer Data be higher than the generation level at which a generating unit's incremental heat rate is minimized (i.e., transitioning from decreasing as output increases to increasing as output increases) except that a Self-Scheduled Resource may modify its Economic Minimum Limit on an hourly basis, as part of its Supply Offer, in order to indicate the desired level of Self-Scheduled MWs.

"Effective Date" is the date that the FERC approves the Settlement Agreement in its entirety without modifications or conditions or with such modifications or changes as are agreed to by the Settling Parties in accordance with Section 2 of the Settlement Agreement.

"Effective Heating Degree Days" is equal to: 68 – (average of max and min Effective Temperature of the day).

"Effective Temperature" is equal to: dry bulb temperature – [windspeed × (65 – dry bulb temp) / 100].

"Existing Capacity" is any Resource that does not meet any of the eligibility criteria for New Capacity as provided in Section 11, Part II.B.3 of the Settlement Agreement or Import Capacity as provided in Section 11, Part II.C.2.a or b of the Settlement Agreement or any Resource that, subject to ISO evaluation, for the purposes of the first FCA, is under construction and within twelve months of its expected commercial operations date as described in Section 11, Part II.D.1 of the Settlement Agreement.

"Existing Import Capacity" is capacity that a party wishes to import in the FCA pursuant to a multi-year contract entered into before the qualification deadline to provide Capacity Resources during the Commitment Period from outside the New England Control Area as described more fully in Section 11, Part II.C.1.a of the Settlement Agreement.

"Export Bid" is a bid submitted in the FCA to export capacity from a Resource.

"Export Capacity" is any Resource within the New England Control Area seeking to submit a bid to export all or part of its capacity in the FCA or selling its Delisted Capacity to a buyer outside the Control Area following the FCA as described in Section 11, Part II.C.1.c of the Settlement Agreement.

"External Resource" is a generation resource located outside the metered boundaries of the New England Control Area.

"FCA Payment" is the payment for which each capacity Resource clearing in the FCA, or otherwise covered by a multi-year commitment, but not a Self-Supplied FCA Resource, shall be entitled to monthly based on the product of its MWs of capacity cleared in the relevant

FCA and the Capacity Clearing Price in the appropriate location in the New England Control Area, as described in more detail in Section 11, Part V.A of the Settlement Agreement.

"Financial Assurance Policy" or **"FAP"** is Exhibit IA, Exhibit IB, or Exhibit IC to Section I of the Tariff, as applicable.

"FERC" or **"Commission"** is the Federal Energy Regulatory Commission.

"Forward Capacity Auction" or **"FCA"** is the descending clock auction that is to be held annually each year in accordance with the Forward Capacity Market as described more fully in Section 11, Part III of the Settlement Agreement.

"Governance Participants" are the parties to the Participants Agreement and the NEPOOL Participants.

"HQI Excess" is the amount by which accepted Import Bids exceed the difference between the approved Phase I/II transfer limit and the approved MW of HQICCs.

"Hydro Quebec Interconnection Capability Credits" or "HQICCs" are credits that are granted to a Market Participant or group of Market Participants in accordance with the ISO System Rules, which may be used to satisfy the Market Participant's UCAP requirement as determined in accordance with Section III.8.2 of Market Rule 1, where the value of such credits is determined in accordance with the ISO New England Manuals.

"Import Bid" is a bid in the FCA to import capacity from outside the New England Control Area, as described in more detail in Section 11, Parts II.C and III.D.4 of the Settlement Agreement.

"Inadequate Supply" is defined in Section 11, Part III.L.2 of the Settlement Agreement.

"Information Policy" is the policy on file with the Commission as part of the Tariff establishing guidelines regarding the information received, created and distributed by Participants and the ISO in connection with the New England Markets and the New England Transmission System.

"Intermittent Resources" are wind, solar and run-of-river hydro Resources, or such other Resources as determined from time to time pursuant to the Participant Processes that provides for consultation with state utility regulatory agencies as described in Section 11, Part II.E.1 of the Settlement Agreement

"Installed Capacity Requirement" or **"ICR"** is the level of capacity required to meet the reliability requirements defined for the New England Control Area and calculated in accordance with Section III.8 of Market Rule 1. The Installed Capacity Requirement is used to determine an Unforced Capacity Requirement for the New England Control Area and individual Market Participants.

"Insufficient Competition" is defined in Section 11, Part III.L.2 of the Settlement Agreement.

"Internal Market Monitoring Unit" is the staff of the ISO designated to implement the mitigation measures set forth in Appendix A to Market Rule 1 for mitigation of market power.

"Local Sourcing Requirement" is the portion of the total capacity requirement of the load in a Capacity Zone that must be purchased from Resources located within that Capacity Zone after taking into account all of the capacity that can be reliably imported into the Capacity Zone.

"Load Serving Entity" or **"LSE"** is an entity that serves load in the New England Control Area.

"Location Forward Reserves Market" or **"LFRM"** is the Locational Forward Reserves Market jointly filed by the ISO and NEPOOL in FERC Docket No. ER06-613-000.

"Locational Marginal Price" or **"LMP"** is as calculated in accordance with Section III.2 of Market Rule 1. The LMP for a Node (as defined in Market Rule 1) is the nodal price at that Node; the LMP for an External Node (as defined in Market Rule 1) is the nodal price at that External Node; the LMP for a Load Zone or Reliability Region (each as defined in Market Rule 1) is the Zonal Price for that Load Zone or Reliability Region, respectively; and the LMP for a Hub (as defined in Market Rule 1) is the Hub Price for that Hub.

"Market Monitor" is ISO's Internal Market Monitoring Unit.

"Market Participant" is a participant in the New England Markets that has executed a Market Participant Service Agreement, or on whose behalf an unexecuted Market Participant Service Agreement has been filed with and accepted or approved by the Commission.

"Market Rule 1" is ISO New England Market Rule 1 and the appendices and attachments thereto set out in Section III of the Tariff, as modified and amended from time to time.

"Market Rules" are the rules for the administration of the New England Markets filed with the Commission in accordance with the Participants Agreement and accepted by the Commission.

"Municipal Market Participant" is a Market Participant that is either a municipality or an agency thereof, or a body politic and public corporation created under the authority of one of the New England states, authorized to own, lease and operate electric generation, transmission

or distribution facilities, or an electric cooperative, or an organization of any such entities.

"NCPC Charge" is the charge to a Market Participant as provided in Section III.3.2.3, Section III.6.4, and Appendix F of Market Rule 1.

"NCPC Credit" is the payment made to a Resource as provided in Section III.3.2.3, Section III.6.4 and Appendix F of Market Rule 1.

"New Capacity" is a Resource which has never been listed as a Capacity Resource (i.e., counted as capacity) in the New England capacity markets or a Resource that meets one of the four criteria listed in Section 11, Part II.B.2 of the Settlement Agreement.

"New Capacity FA Amount" is the financial assurance obligation of New Capacity whose bid has been accepted in the FCA equal to CONE (on a $/kw-month basis) for that FCA multiplied by the number of kw of capacity awarded, as described in Section 11, Part II.G.2.b of the Settlement Agreement.

"New England Control Area" is the Control Area (as defined in Section II.1.11 of the Tariff) for New England, which includes PTF, Non-PTF, MTF and OTF. The New England Control Area covers Connecticut, Rhode Island, Massachusetts, New Hampshire, Vermont, and part of Maine (i.e., excluding the portions of Northern Maine and the northern portion of Eastern Maine which are in the Maritimes Control Area).

"New England Markets" are the markets for the purchase of energy, capacity, ancillary services, demand response services, or other related products or services (including financial transmission rights) within the New England Control Area, as set forth in the Market Rule 1.

"New Import Capacity" is capacity that a party wishes to import in the FCA but without a multi-year contract before the qualification deadline to provide Ca-

pacity Resources during the Commitment Period from outside the New England Control Area as described in Section 11, Part II.C.1.b of the Settlement Agreement.

"Offer" is the amount a Supply Offer would have been but for the Offer Cap as set forth in Section 11, Part IV.A.5 of the Settlement Agreement.

"Offer Cap" is the amount defined in Section 1.10.1A(d)(viii) of Market Rule 1 above which an energy offer price may not be specified.

"Operating Day" is a calendar day period beginning at midnight for which transactions in the New England Markets are scheduled.

"Out of Market Bid" is a New Capacity Bid or a New Import Bid that, pursuant to Section 11, Part III.H.2 of the Settlement Agreement, is not allowed by the Market Monitor to set the Capacity Clearing Price.

"Participant Processes" shall mean those processes for Governance Participants outlined in Section 7.1.1 of the Participants Agreement.

"Peak Energy Rent" or **"PER"** is the amount determined in accordance with Section 11, Part V.B of the Settlement Agreement.

"Permanent De-list Bid" is a bid from Existing Capacity submitted in the FCA to be permanently removed from the Forward Capacity Market, as described in more detail in Section 11, Part III.D.3 of the Settlement Agreement.

"Pool-Planned Unit" is one of the following units: New Haven Harbor Unit 1 (Coke Works), Mystic Unit 7, Canal Unit 2, Potter Unit 2, Wyman Unit 4, Stony Brook Units 1, 1A, 1B, 1C, 2A and 2B, Millstone Unit 3, Seabrook Unit 1 and Waters River Unit 2 (to the extent of 7 MWs of its Summer Capability and 12 MWs of its Winter Capability).

"Poorly Performing Unit" is a Resource which, for purposes of qualifying to participate in the FCA, in any four-year period (a) receives three availability scores of less than or equal to forty percent (40 percent), and (b) fails to be available during at least ten (10) Shortage Events, as described in more detail in Section 11, Part V.C.7 of the Settlement Agreement.

"Power Year" is a period of twelve (12) months commencing on June 1 of each year and ending on May 31 of the next calendar year.

"Qualified Capacity" for the FCA and annual reconfiguration actions: (a) for New Capacity, is an amount in MWs equal to such New Capacity's bid MWs, subject to demonstrations of at least that capacity in the qualification process; (b) for Existing Capacity, except as provided in Section 11, Part II.D.5 of the Settlement Agreement, is an amount in MWs equal to its Summer Seasonal Claimed Capability as adjusted pursuant to Section II.D.4 of the Settlement Agreement; (c) for Intermittent Resources and Demand Resources is the amount in MWs to be determined pursuant to the distinct method to be developed by the end of the fourth quarter of 2006 pursuant to the Participant Processes that includes consultation with state utility regulatory agencies.

"Real-Time" is a period in the current Operating Day for which the ISO dispatches Resources for energy and Regulation (as defined in Market Rule 1), designates Resources for Regulation and, if necessary, commits additional Resources.

"Real-Time Energy Market" is the purchase or sale of energy, payment of congestion costs, and payment for losses for quantity deviations from the Day-Ahead Energy Market in the Operating Day.

"Reserve Constraint Penalty Factors" or **"RCPFs"** are rates, in $/MWh, that are used within the Real-Time

dispatch and pricing algorithm to reflect the value of operating reserve shortages and are defined in Section III.2.8 of Market Rule 1.

"Resource" is a generating unit, a Dispatchable Load, an External Resource, or an External Transaction as defined in Market Rule 1.

"Resource Adequacy Assessment" or **"RAA"** is the assessment performed periodically by the ISO for each hour of each day in connection with system operations, as referred to in Section 11, Part VII.A of the Settlement Agreement.

"Seasonal Claimed Capability" is the maximum dependable load-carrying ability in kilowatts of a generating unit (or ISO-approved combination of units, as per OP 14) being rated, excluding capacity required for station use, for the Summer Period or Winter Period, as applicable.

"Self-Schedule" is the action of a Market Participant in committing and/or scheduling its Resource, in accordance with applicable ISO New England Manuals, to provide service in an hour, whether or not in the absence of that action the Resource would have been scheduled or dispatched by the ISO to provide the service.

"Self-Supplied FCA Resource" is defined in Section 11, Part II.F.1 of the Settlement Agreement.

"Self-Supply Option" is defined in Section II, Part II.F of the Settlement Agreement.

"Settlement Agreement" is the Settlement Agreement Resolving all Issues dated March 6, 2006 in Docket No. ER03-563-____.

"Settling Party" [is] a party to the Settlement Agreement.

"Shortage Event" is defined in Section 11, Part V.C.1.d of the Settlement Agreement.

"Successful FCA" is a FCA that has not been found to have Insufficient Competition or Inadequate Supply.

"Summer Period" is for each Power Year the four-month period from June through September.

"Supplemental Reserves" are the additional 1,000 MW of NCPC scheduled in accordance with Section 11, Part VII.D of the Settlement Agreement by the ISO if and as needed.

"Tariff" is the ISO New England Transmission, Markets and Services Tariff, FERC Electric Tariff No. 3.

"Term Sheet" is the confidential document voted upon by the settling parties dated January 31, 2006 that was referenced in the Report filed by the Settlement Judge with the FERC on January 31, 2006 in Docket No. ER03-563-055.

"Transition Period" is the period of time commencing on December 1, 2006 and ending May 30, 2010, or as provided in Section 11, Part VIII.I.

"Unforced Capacity" or **"UCAP"** is the measure by which: (1) Installed Capacity suppliers will be rated, in accordance with the formulae set forth in the ISO New England Manuals, to quantify the extent of their contribution to satisfy the ISO Installed Capacity Requirement, and (2) the measure to determine if a Market Participant has met its procurement obligations relating to the Installed Capacity Requirement.

"Waiver Period" is the period of time from March 6, 2006 through the earlier of September 5, 2006, or the date on which the second FCA is successfully completed.

"Winter Period" is for each Power Year the eight-month period from October through May.

TABLE OF ABBREVIATIONS AND ACRONYMS

This Table provides definitions for abbreviations and acronyms used throughout the Settlement Agreement and related materials.

2d RNA	Second Restated NEPOOL Agreement
AGC	Automatic Generation Control
ARRs	Auction Revenue Rights
CONE	Cost of New Entry
CTRs	Capacity Transfer Rights
DCAs	Designated Congestion Areas
EcoMin	Economic Minimum Limit
EFORd	Demand Estimated Forced Outage Rate
FAP	Financial Assurance Policy
FCA	Forward Capacity Auction
FCM	Forward Capacity Market
FERC	Federal Energy Regulatory Commission
FPA	Federal Power Act
HQICCs	Hydro Quebec Interconnection Capability Credits
ICR	Installed Capacity Requirement
IRH	Interconnection Rights Holders
ISO	ISO New England Inc.
kW	Kilowatt
LFRM	Locational Forward Reserves Market
LICAP	Locational Installed Capacity
LMP	Locational Marginal Price
LSE	Load Serving Entity
MMWEC	Massachusetts Municipal Wholesale Electric Company

Mobile-Sierra	"public interest" standard of review (set forth in *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332 (1956) and *Federal Power Commission v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956))
MTF	Merchant Transmission Facilities
MW	Megawatt
NCPC	Net Commitment Period Compensation
NEMA	Northeast Massachusetts
NEPOOL	New England Power Pool
NYPA	New York Power Authority
OMOI	FERC Office of Market Oversight and Investigations
OP	Operating Procedure
OP-4	Operating Procedure 4, entitled "Action During a Capacity Deficiency"
OP-7	Operating Procedure 7, entitled "Action in an Emergency"
OTF	Other Transmission Facility
PER	Peak Energy Rent
PTF	Pool Transmission Facilities
RAA	Resource Adequacy Assessment
RCPFs	Reserve Constraint Penalty Factors
RFP	Request for Proposal
RMR	Reliability Must Run
RNA	Restated NEPOOL Agreement
ROCT	Rest of Connecticut
ROP	Rest of Pool
RSP	Regional System Plan
SWCT	Southwest Connecticut

UCAP	Unforced Capacity
WRC	Wellesley, Reading and Concord

PETITIONER'S BRIEF

133

(8)

No. 08-674

Supreme Court, U.S.
FILED
JUL 7 - 2009
OFFICE OF THE CLERK

IN THE

Supreme Court of the United States

NRG POWER MARKETING, LLC, *ET AL.*,
Petitioners,

v.

MAINE PUBLIC UTILITIES COMMISSION, *ET AL.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

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QUESTION PRESENTED

The Federal Power Act, 16 U.S.C. §§ 791a *et seq.*, requires that rates for the sale of electricity in interstate commerce be "just and reasonable." Under the *Mobile-Sierra* doctrine—named for this Court's decisions in *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956), and *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956)—the Federal Energy Regulatory Commission ("FERC") must "presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law," and that "presumption may be overcome only if FERC concludes that the contract seriously harms the public interest." *Morgan Stanley Capital Group Inc.* v. *Pub. Util. Dist. No. 1*, 128 S. Ct. 2733, 2737 (2008). In the decision below, the court of appeals held that, "when a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply." Pet. App. 22a. The question presented is:

Whether *Mobile-Sierra*'s public-interest standard applies when a contract rate is challenged by an entity that was not a party to the contract.

PARTIES TO THE PROCEEDINGS BELOW

Petitioners NRG Power Marketing, LLC (formerly NRG Power Marketing, Inc.), Devon Power LLC, Connecticut Jet Power LLC, Norwalk Power LLC, Middletown Power LLC, Montville Power LLC, and Somerset Power LLC intervened in the court of appeals and were parties in proceedings before the Federal Energy Regulatory Commission.

The following parties before the Federal Energy Regulatory Commission also intervened for the respondent in the court of appeals: Connecticut Department of Public Utility Control; TransCanada Power Marketing, Ltd.; International Power America, Inc.; Bridgeport Energy, LLC; Casco Bay Energy Co., LLC; NEPOOL Participants Committee; Milford Power Co., LLC; FPL Energy, LLC; Entergy Nuclear Generation Co., LLC; Entergy Nuclear Vermont Yankee, LLC; Mirant Energy Trading, LLC; Mirant Kendall, LLC; Mirant Canal, LLC; Boston Generation, LLC; Mystic I, LLC; Mystic Development, LLC; Fore River Development, LLC; Massachusetts Municipal Wholesale Electric Co.; Connecticut Municipal Electric Energy Cooperative; ISO New England, Inc.; Lake Road Generating Co.; Berkshire Power Co., LLC; MASSPOWER; Dominion Resources, Inc.; Dominion Energy Marketing, Inc.; Dominion Nuclear Connecticut, Inc.; Central Vermont Public Service Co.; PSEG Power, LLC; and PSEG Energy Resources & Trade LLC.

The Federal Energy Regulatory Commission was the respondent in the court of appeals and is therefore a respondent here under this Court's Rule 12.6.

Respondents Maine Public Utilities Commission, the Attorney General of Massachusetts, and the Attorney General of Connecticut were the petitioners in the court

of appeals and parties before the Federal Energy Regulatory Commission.

Respondents Industrial Energy Consumer Group, NEPOOL Industrial Customer Coalition, and NSTAR Electric & Gas Corp. were intervenors in the court of appeals and parties before the Federal Energy Regulatory Commission.

CORPORATE DISCLOSURE STATEMENT

Pursuant to this Court's Rule 29.6, petitioners NRG Power Marketing, LLC, Devon Power LLC, Connecticut Jet Power LLC, Norwalk Power LLC, Middletown Power LLC, Montville Power LLC, and Somerset Power LLC state that they are subsidiaries of NRG Energy, Inc. and that they have no outstanding shares of stock owned by the public. NRG Energy, Inc. is a Delaware corporation whose common stock is held by the public. NRG Energy, Inc. has no parent company and no publicly held company has a 10 percent or greater ownership in NRG Energy, Inc.

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IN THE

Supreme Court of the United States

No. 08-674

NRG POWER MARKETING, LLC, *ET AL.*,
Petitioners,

v.

MAINE PUBLIC UTILITIES COMMISSION, *ET AL.*,
Respondents.

On Writ of Certiorari
to the United States Court of Appeals
for the District of Columbia Circuit

BRIEF FOR PETITIONERS

DECISIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-27a) is reported at 520 F.3d 464. The decision of the Federal Energy Regulatory Commission (Pet. App. 102a-223a) is reported at 115 F.E.R.C. ¶61,340, and the Commission's decision on rehearing (Pet. App. 28a-101a) is reported at 117 F.E.R.C. ¶61,133.

JURISDICTION

The court of appeals entered judgment on March 28, 2008. The court denied rehearing and rehearing *en banc* on October 6, 2008. Pet. App. 241a-248a. The petition for a writ of certiorari was filed November 21, 2008, and

granted April 27, 2009. This Court has jurisdiction under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

Relevant provisions of the Federal Power Act, ch. 687, 49 Stat. 803 (1935) (codified as amended at 16 U.S.C. §§ 791a *et seq.*), are set forth at Pet. App. 251a-261a.

INTRODUCTION

The *Mobile-Sierra* doctrine requires the Federal Energy Regulatory Commission ("FERC") to "presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law." *Morgan Stanley Capital Group Inc.* v. *Pub. Util. Dist. No. 1*, 128 S. Ct. 2733, 2737 (2008). That presumption can be overcome only in "extraordinary circumstances where the public will be severely harmed." *Id.* at 2749. Those longstanding restrictions on FERC's authority to set aside contract rates reflect the critical importance of contract stability in volatile energy markets, where suppliers must routinely commit hundreds of millions of dollars to build generating capacity—investments that can take decades to recover. "Competitive power markets simply cannot attract the capital needed to build adequate generating infrastructure without regulatory certainty, including certainty that the Commission will not modify market-based contracts unless there are *extraordinary* circumstances." *Nev. Power Co.* v. *Duke Energy Trading & Mktg., L.L.C.*, 99 F.E.R.C. ¶61,047, at 61,190 (2002). "By preserving the integrity of contracts," *Mobile-Sierra* "permits the stability of supply arrangements which all agree is essential to the health of the * * * industry." *United Gas Pipe Line Co.* v. *Mobile Gas Serv. Corp.*, 350 U.S. 332, 344 (1956).

The court below held that, "when a rate challenge is brought by a non-contracting third party, the *Mobile-*

Sierra doctrine simply does not apply." Pet. App. 22a. Under that holding, *Mobile-Sierra* protects contracts from challenges by a contracting counterparty, but *any other entity* indirectly affected by a contract rate—any consumer, advocacy group, state utility commission, or elected official acting *parens patriae*—can challenge the rate without regard to *Mobile-Sierra*'s protections. Because that holding is inconsistent with this Court's precedents and threatens to reduce *Mobile-Sierra* to a historical footnote, the judgment below should be reversed.

STATEMENT

I. STATUTORY BACKGROUND

A. The Federal Power Act

The Federal Power Act ("FPA"), 16 U.S.C. §§ 791a *et seq.*, gives FERC exclusive authority to regulate the "sale of electric energy at wholesale in interstate commerce." 16 U.S.C. § 824(b)(1); see *New England Power Co.* v. *New Hampshire*, 455 U.S. 331, 340 (1982). The Act provides that "[a]ll rates and charges" subject to FERC's jurisdiction "shall be just and reasonable," and declares that any "rate or charge that is not just and reasonable is * * * unlawful." 16 U.S.C. § 824d(a). The Act also forbids any "undue preference or advantage" or any "unreasonable difference" in rates. *Id.* § 824d(b).

Traditionally, wholesale energy rates have been set in two ways. First, a supplier may set rates "unilaterally by tariff," offering to sell electricity to buyers on terms the supplier determines. See *Morgan Stanley Capital Group Inc.* v. *Pub. Util. Dist. No. 1*, 128 S. Ct. 2733, 2737-2738 (2008). Alternately, buyers and sellers can agree on rates by "contract." See *id.* at 2738.

Consistent with those two methods, Section 205 of the FPA requires suppliers to file with the Commission

"schedules showing all rates and charges," together with "all contracts" related to the suppliers' rates. 16 U.S.C. §§824d(c), (d). FERC need not approve the filing for a rate to become effective. But FERC may conduct a hearing into the rate's lawfulness "either upon complaint or upon its own initiative without complaint," and can reject any rate it finds unlawful. See *id.* §824d(e).

While Section 205 authorizes FERC to reject new rates, Section 206 empowers FERC to modify existing ones: "Whenever the Commission, after a hearing held upon its own motion or upon complaint, shall find that any rate * * * or contract affecting such rate * * * is unjust, unreasonable, unduly discriminatory or preferential, the Commission shall determine the just and reasonable rate * * * or contract * * * and shall fix the same by order." 16 U.S.C. §824e(a). FERC can order refunds of certain amounts paid after such a proceeding begins. *Id.* §824e(b).

B. The *Mobile-Sierra* Doctrine

The *Mobile-Sierra* doctrine originated in this Court's twin decisions in *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956) ("*Mobile*"), and *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956) ("*Sierra*"). Those cases interpreted the statutory phrase "just and reasonable" in the context of rates set by the parties through contract rather than by the seller through unilateral tariff.

1. In *Mobile*, a natural gas supplier (United) had contracted to provide gas to a distributor (Mobile) for ten years at a fixed rate. 350 U.S. at 335-336.[1] Several years

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[1] Although *Mobile* arose under the Natural Gas Act rather than the FPA, see 350 U.S. at 333-337, the two statutes are "virtually identical" in relevant respects, *id.* at 346, and this Court's "established

into the contract, United filed schedules with the Federal Power Commission (FERC's predecessor) purporting to raise Mobile's rates. *Id.* at 336. This Court held the filing invalid. *Id.* at 347. The Act, the Court stated, "evinces no purpose to abrogate private rate contracts." *Id.* at 338. "To the contrary, by requiring contracts to be filed with the Commission, the Act expressly recognizes that rates to particular customers may be set by individual contracts." *Ibid.* The Act thus differed from statutes such as the Interstate Commerce Act, which required uniform tariffs. See *id.* at 338-339. "Absent the Act," the Court noted, "a unilateral announcement of a change to a contract would of course be a nullity." *Id.* at 339. The statutory filing requirement did not affect that result. "Th[at] section says only that a change *cannot* be made without the proper notice to the Commission; it does not say under what circumstances a change *can* be made." *Ibid.*

The Court explained that, although the Act authorizes the *Commission* to modify contract rates, the Commission can exercise that power only "when necessary in the public interest"—not for the "private interests" of the contracting parties. See 350 U.S. at 344. "By preserving the integrity of contracts," the Act "permits the stability of supply arrangements which all agree is essential to the health of the natural gas industry." *Ibid.* Contracting parties must often undertake "substantial investments which [they] would be unwilling to make without long-term commitments." *Ibid.* "[A]nd the distributor can hardly make such commitments if its supply contracts are subject to unilateral change by the natural gas com-

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practice" is to "cit[e] interchangeably decisions interpreting the pertinent sections of the two statutes," *Ark. La. Gas Co.* v. *Hall*, 453 U.S. 571, 577 n.7 (1981).

pany whenever its interests so dictate." *Ibid.* United's filing was thus a "nullity," and "the contract rate remained the only lawful rate." *Id.* at 347.

2. Announced the same day as *Mobile*, *Sierra* involved an electricity supplier's similar attempt to raise rates several years into a contract. 350 U.S. at 351-352. The Commission had allowed the new rate to take effect, commenting that the contract rate was "'unreasonably low and therefore unlawful'" because it produced an inadequate return. *Id.* at 352, 354. Citing *Mobile*, the Court found the unilateral filing ineffective under Section 205. *Id.* at 353. Unlike in *Mobile*, however, the Commission had found the prior rate "unlawful," arguably exercising its Section 206 power to set aside unjust or unreasonable rates. See *ibid.*

This Court held that the Commission had erred by deeming the contract rate unreasonable "solely because it yield[ed] less than a fair return." 350 U.S. at 354-355. "[W]hile it may be that the Commission may not normally *impose* upon a public utility a rate which would produce less than a fair return, it does not follow that the public utility may not itself agree by contract to a rate affording less than a fair return or that, if it does so, it is entitled to be relieved of its improvident bargain." *Id.* at 355. "[T]he sole concern of the Commission would seem to be whether the rate is so low as to adversely affect the *public interest*—as where it might impair the financial ability of the public utility to continue its service, cast upon other consumers an excessive burden, or be unduly discriminatory." *Ibid.* (emphasis added). The Court held that "the purpose of the power given the Commission by § 206(a) is the protection of the public interest, as distinguished from the private interests of the utilities." *Ibid.* Accordingly, "a contract may not be said to be either 'un-

just' or 'unreasonable' simply because it is unprofitable to the public utility." *Ibid.*

3. That principle—that FERC cannot abrogate contract rates absent a sufficient showing of harm to the "public interest" (as opposed to the private interests of contracting parties)—has come to be known as the "*Mobile-Sierra*" doctrine. Just two Terms ago, in *Morgan Stanley Capital Group Inc.* v. *Public Utility District No. 1*, 128 S. Ct. 2733 (2008), this Court reiterated that *Mobile-Sierra* requires FERC to "presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law," and that this "presumption may be overcome only if FERC concludes that the contract seriously harms the public interest." *Id.* at 2737. The Court held that the demanding standard applicable to contract rates—known as the "public interest standard"—applies whether the complainant urges that the price is too high or too low. See *id.* at 2747-2749. And the Court rejected the Ninth Circuit's ruling that the more flexible standard applicable to a seller's unilateral tariff (best referred to as the "ordinary just-and-reasonable standard," see *id.* at 2740) applies to contract rates absent FERC's prior approval of the contract at issue. See *id.* at 2745-2747.

The *Mobile-Sierra* doctrine reflects "the commonsense notion that '[i]n wholesale markets, the party charging the rate and the party charged [are] often sophisticated businesses enjoying presumptively equal bargaining power, who could be expected to negotiate a "just and reasonable" rate as between the two of them.'" *Morgan Stanley*, 128 S. Ct. at 2746 (quoting *Verizon Commc'ns Inc.* v. *FCC*, 535 U.S. 467, 479 (2002)). It also reflects the "important role of contracts in the FPA" in providing a "key source of stability" that "ultimately

benefits consumers." *Id.* at 2749. "'[U]ncertainties regarding rate stability and contract sanctity can have a chilling effect on investments and a seller's willingness to enter into long-term contracts and this, in turn, can harm customers in the long run.'" *Ibid.* (quoting *Market-Based Rates*, 72 Fed. Reg. 39,904, 39,906 (2007)).

Consistent with *Mobile-Sierra*'s emphasis on contracts, an agreement can *prescribe* a more lenient standard under which FERC (or the parties) can modify the agreed-upon rates. See *Morgan Stanley*, 128 S. Ct. at 2739. Such provisions are known as "*Memphis* clauses," after *United Gas Pipe Line Co.* v. *Memphis Light, Gas & Water Division*, 358 U.S. 103 (1958). Absent a *Memphis* clause, however, FERC's authority is limited: FERC can abrogate contract rates only in "extraordinary circumstances where the public will be severely harmed." *Morgan Stanley*, 128 S. Ct. at 2749.

II. This Litigation

A. The New England Capacity Market

This case arises out of efforts to ensure that New England has sufficient electrical generating capacity to meet demand. Roughly speaking, "capacity" is the *ability* to produce electricity as opposed to electricity itself. See *Conn. Dep't of Pub. Util. Control* v. *FERC*, Nos. 07-1375 *et al.*, 2009 WL 1754607, at *1 (D.C. Cir. June 23, 2009). Utilities purchase capacity from generators to ensure that the system has adequate electricity resources to meet demand at all times, averting blackouts or other reliability problems. See Pet. App. 2a. A utility purchasing capacity is essentially paying to ensure that electricity is available whether or not that electricity is ultimately used. See *ibid.*

New England's electric utilities have long integrated their transmission systems so that capacity in one area can be used to meet demand elsewhere. See, *e.g.*, *NEPOOL Power Pool Agreement*, 48 F.P.C. 538 (1972). In 1998, they created an independent entity—the New England Independent System Operator ("ISO-NE")—to manage those systems. See Pet. App. 3a & n.2; *New England Power Pool*, 83 F.E.R.C. ¶61,045 (1998).

New England's capacity market, however, was "rife with problems." Pet. App. 2a. The incentives to retain or attract generating capacity were insufficient. "'[E]xisting generators needed for reliability [we]re not earning sufficient revenues (and [we]re in fact losing money), and * * * additional infrastructure [wa]s needed soon to avoid violations of reliability criteria.'" *Ibid.* That deficiency had "persisted and gr[own]." *Id.* at 99a.

B. Proceedings Before FERC

ISO-NE struggled to resolve those problems. See Pet. App. 2a-5a. FERC largely rejected one approach, involving so-called "Reliability Must-Run" agreements, in 2003. See *id.* at 2a-3a. A FERC administrative law judge approved another proposal, which set prices using an "administratively-determined demand curve," in 2005. See *id.* at 4a-5a. But it too was "extremely controversial." *Id.* at 4a.

1. *The Settlement Agreement*

Finally, after four months of negotiations involving 115 parties, a settlement was reached. Pet. App. 110a. Of the 115 parties, eight opposed the settlement. *Ibid.* And only one of those eight—NSTAR Electric and Gas Corporation—is a utility that participates in the wholesale capacity market. See *id.* at 121a n.32. The other seven objectors—the Maine Public Utilities Commission and Public Advocate, the attorneys general of Connecti-

cut and Massachusetts, two industrial consumer interest groups, and a consortium—are all at most indirectly affected by wholesale rates. See *id.* at 120a-121a & nn.31-32, 144a. A wide array of parties supported the settlement, including a host of power-purchasing utilities and power-supplying generators, ISO-NE, the Connecticut Department of Public Utility Control and Office of Consumer Counsel, and the public utility commissions of New Hampshire, Rhode Island, and Vermont. See *id.* at 220a-221a; J.A. 89-91.

To redress the market's prior failure to attract sufficient capacity, the agreement created a "Forward Capacity Market" in which annual auctions are used to meet demand. See Pet. App. 110a-116a; J.A. 97-160. Each auction takes place three years before the capacity will be needed. J.A. 98. Suppliers bid to provide capacity for a period of one year (or up to five years in the case of new entrants) after that three-year lead time. See *id.* at 98-99, 105. The three-year lead time exists so that bidders can build new generating facilities, thus allowing new entrants to compete with existing suppliers in the auction. See Pet. App. 110a; J.A. 68-69. At the end of the auction, the winning bidders are committed to supply capacity at the auction's "clearing price." See Pet. App. 110a; J.A. 66, 149. ISO-NE must file the auction results with FERC under Section 205, and interested parties have 45 days to challenge them. J.A. 118. Market participants are not required to buy or sell capacity at the auction price. Rather, utilities can contract for capacity in advance of and outside the auction (or commit to generate power themselves) and thereby "meet [their] capacity obligations without paying the auction clearing price." Pet. App. 112a; see p. 49, *infra*. Utilities that choose to acquire capacity through the auction, however, are re-

sponsible for paying for capacity at the auction price in proportion to their share of peak usage. See Pet. App. 112a; J.A. 70.[2]

The settlement also provides for "transition payments" to purchase necessary capacity until the capacity from the auctions becomes available. See Pet. App. 116a-118a; J.A. 163-169. Those fixed-rate payments, which run through May 31, 2010, see J.A. 164, were designed to "serve as a bridge" and to "help ensure that existing generators remain available until new resources can be built" based on the auction results. See Pet. App. 117a. ISO-NE's consumer-serving utilities (also known as "load-serving entities") are responsible for the transition payments in proportion to their share of peak usage. See *ibid.*; J.A. 163.

This case concerns the standard that will govern *future* challenges to the rates agreed upon as a result of the auction process and the transition payments set by the settlement agreement. The agreement includes a broad *Memphis* clause stating that, except as "expressly provided," the agreement "does *not* impose the *Mobile-Sierra* standard." J.A. 95 (emphasis added); see also *id.* at 58; Br. in Opp. 6. It provides two exceptions. First, the *Mobile-Sierra* public-interest standard applies to rates agreed upon through the capacity auctions (except during the 45-day review period following each auction, when the ordinary just-and-reasonable standard applies, see Pet. App. 78a, 120a, 202a). See J.A. 95. Second, the public-interest standard applies to the transition payments (and their implementing rules) following FERC's ap-

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[2] In addition, buyers and sellers can exchange capacity obligations in periodic "reconfiguration" auctions. See J.A. 137-142.

proval of the settlement. See *ibid.*[3] That *Mobile-Sierra* standard, the agreement continues, applies "whether the change is proposed by a Settling Party, a non-Settling Party, or the FERC acting *sua sponte*." *Ibid.* The settlement's explanatory statement notes that "one purpose for adopting the *Mobile-Sierra* standard for final auction prices is to reduce regulatory uncertainty and thus the risk premium that new entrants may require." *Id.* at 60-61.

2. *FERC's Decisions*

The parties filed the proposed settlement with the Commission. Pet. App. 103a. As the parties agreed, FERC reviewed the settlement under the ordinary just-and-reasonable standard, not *Mobile-Sierra*'s public-interest standard, see *id.* at 140a-144a, unanimously approving it as an effective way to "resolve the deficiencies in New England's existing capacity market," *id.* at 135a, 219a. "[A]s a package," FERC found, the agreement "achieves an overall just and reasonable result within a zone of reasonableness." *Id.* at 141a-142a.

FERC lauded the capacity auctions as a "market-based mechanism" that would "appropriately value capacity resources based on their location." Pet. App. 138a. The auctions would "provide appropriate signals to investors when new infrastructure resources are necessary with sufficient lead time to allow that infrastructure to be put into place before reliability is sacrificed." *Ibid.*

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[3] The agreement thus states that "the 'public interest' standard of review set forth in [*Mobile*] and [*Sierra*]" governs "(i) challenges to the Capacity Clearing Prices derived through the [Forward Capacity Auctions] and prices resulting from reconfiguration auctions," and "(ii) proposed changes to * * * [the] Agreements Regarding Transition Period[ ] and the Market Rules implementing that part" following the agreement's "Effective Date." J.A. 95.

FERC also found the transition payments to be "within a range that * * * is just and reasonable." *Id.* at 143a.

Most important here, FERC held that the *Mobile-Sierra* public-interest standard could govern future challenges to auction rates and transition payments regardless of the challenger. FERC rejected the claim that applying *Mobile-Sierra* to challenges by non-contracting third parties would "'disenfranchise[]'" them from "'the protections against unjust and unreasonable rates provided in the FPA.'" Pet. App. 194a. FERC stressed the narrow scope of the provision, which addressed only two discrete sets of prices. See *id.* at 200a. And it noted that it had "routinely permitted the use of similar provisions in settlement agreements, including contested settlements." *Id.* at 200a & n.150 (collecting cases).

FERC explained that the stability provided by *Mobile-Sierra* was "particularly important in this case, which was initiated in part because of the unstable nature" of the existing market. Pet. App. 202a. "The Court's statement in *Mobile* that 'all agree . . . [that] the stability of supply arrangements . . . is essential to the health of the natural gas industry' is no less true with regard to the health of New England's electricity infrastructure." *Id.* at 203a (quoting 350 U.S. at 344). At the same time, the "limited *Mobile-Sierra* provision appropriately balances the need for rate stability and the interests of the diverse entities" affected. *Id.* at 202a. And FERC could still vindicate third parties' interests because "'[t]he *Mobile-Sierra* doctrine itself allows for intervention by FERC where it is shown that the interests of third parties are threatened.'" *Id.* at 201a (quoting *Ne. Utils. Serv. Co.* v. *FERC*, 993 F.2d 937, 961 (1st Cir. 1993)).

FERC later denied rehearing. Pet. App. 28a-101a. FERC rejected arguments that the matters covered by the *Mobile-Sierra* clause were not "contracts" to which *Mobile-Sierra* applied, *id.* at 70a-71a, 75a-76a, and that *Mobile-Sierra* could not apply to challenges by non-contracting parties, *id.* at 76a-79a.

C. The Court of Appeals' Decision

The D.C. Circuit upheld FERC's order in nearly all respects, but granted the petition for review with respect to applying the *Mobile-Sierra* standard to auction rates and transition payments. Pet. App. 1a-27a. Applying that standard to future challenges by non-contracting third parties, the court held, would "deprive them of their statutory right to challenge rates under the 'just and reasonable' standard." *Id.* at 19a.

The court recognized that, "[u]nder the *Mobile-Sierra* doctrine, 'FERC may abrogate or modify freely negotiated private contracts * * * only if required by the public interest.'" Pet. App. 19a. FERC must apply "a strong presumption that the settled rate is just and reasonable" and "may only set aside the contract for the most compelling reasons." *Id.* at 20a. That public-interest standard, the court noted, is "'much more restrictive'" than the standard that governs unilateral tariffs. See *id.* at 19a. That different treatment of contract rates "recognizes the superior efficiency of private bargaining." *Ibid.*

The court of appeals held, however, that *Mobile-Sierra*'s public-interest standard could not be applied to "rate challenges brought by non-contracting third parties." Pet. App. 20a. The court observed that, "when a party files a complaint against a rate or charge, FERC must adjudicate the challenge under the 'just and reasonable' standard." *Ibid.* (quoting 16 U.S.C. § 824e(a)). The court asserted that *Mobile-Sierra* "carves out an exception to

this rule based on the 'familiar dictates of contract law.'" *Ibid.* Relying on that understanding, the court held that the doctrine applies only where "'one party to a rate contract on file with FERC attempts to effect a unilateral rate change'"—not where a non-contracting party challenges a rate agreed to by contracting parties. See *id.* at 22a.

The court of appeals did not explain why *Mobile-Sierra*'s presumption of reasonableness (or the rationales underlying it) would cease to apply merely because a non-contracting party brought the challenge. Instead, quoting a case that addressed whether an arbitration agreement precludes non-signatories from seeking judicial relief, the court stated that "'a contract cannot bind a non-party.'" Pet. App. 22a (quoting *EEOC* v. *Waffle House, Inc.*, 534 U.S. 279, 294 (2002)). The court asserted that the settlement, by requiring application of *Mobile-Sierra*, improperly "attempt[ed] to thrust the 'public interest' standard of review upon non-settling third parties." *Ibid.* "[W]hen a rate challenge is brought by a non-contracting third party," the court concluded, "the *Mobile-Sierra* doctrine simply does not apply; the proper standard of review remains the 'just and reasonable' standard in section 206 of the Federal Power Act." *Ibid.* Even though the *Mobile-Sierra* provision was of "'limited' applicability," the court continued, applying *Mobile-Sierra*'s public-interest standard to non-parties would still "deprive[] [them] of their statutory right to have rate challenges adjudicated under the 'just and reasonable' standard." *Ibid.*

The court acknowledged that FERC had repeatedly approved similar provisions in the past, but it deemed those decisions irrelevant because they had not been judicially approved. Pet. App. 23a. In any event, the court

asserted, those FERC decisions contravened the statutory text, which "quite clear[ly]" directs FERC to determine whether rates are "'unjust [or] unreasonable.'" *Id.* at 24a. The court stated that *Mobile-Sierra* is designed only "to ensure contract stability *as between the contracting parties—i.e.*, to make it more difficult for either party to shirk its contractual obligations." *Ibid.* Seeking to protect stability by applying the doctrine to third parties, the court claimed, "makes no sense." *Ibid.*

D. This Court's Intervening Decision in *Morgan Stanley* and the Denial of Rehearing

Shortly after the court of appeals' decision, this Court decided *Morgan Stanley*. In that case, the Court addressed (among other things) the relationship between *Mobile-Sierra*'s public-interest standard and the statutory requirement of "just and reasonable" rates. The Court acknowledged that lower federal courts and FERC had come to distinguish the *Mobile-Sierra* "public interest standard" applicable to contract rates from the "just and reasonable standard." 128 S. Ct. at 2740. But the Court declined to "take this nomenclature to stand for the obviously indefensible proposition that a standard different from the statutory just-and-reasonable standard applies to contract rates." *Ibid.* "Rather, the term 'public interest standard' refers to the differing *application* of that just-and-reasonable standard to contract rates." *Ibid.* *Mobile-Sierra*, the Court explained, simply "provide[s] a definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context." *Id.* at 2746.

FERC and other parties then sought rehearing of the decision below, urging that *Morgan Stanley* foreclosed the panel's holding that *Mobile-Sierra* was an "'exception'" to the statutory just-and-reasonable standard and

that applying *Mobile-Sierra* would "'deprive[] non-settling parties of their statutory right to have rate challenges adjudicated under the "just and reasonable" standard.'" FERC Reh'g Pet. in Nos. 06-1403 *et al.*, at 5-6 (D.C. Cir. Aug. 8, 2008). *Mobile-Sierra*'s public-interest standard could not "deprive" anyone of their statutory right to "just and reasonable" review, FERC explained, because—as *Morgan Stanley* makes clear—the public-interest standard is merely an "'*application* of the just-and-reasonable standard to contract rates.'" *Ibid.* Stressing that this was the first time it had sought rehearing in almost five years, *id.* at 2 & n.2, FERC highlighted the serious consequences of the panel's error. The panel decision, FERC urged, "undermines the contract certainty needed for infrastructure investment emphasized in *Morgan Stanley*" and produces a "manifestly anomalous result." *Id.* at 11-12.[4]

The court of appeals denied rehearing. Pet. App. 241a-248a. On April 27, 2009, this Court granted the petition for a writ of certiorari. 129 S. Ct. 2050.

SUMMARY OF ARGUMENT

1. The *Mobile-Sierra* doctrine has protected the stability of contractual relations in the energy industry for

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[4] Two Commissioners dissented from FERC's decision to seek rehearing. Pet. App. 224a-240a. Their dissent, however, did not defend the D.C. Circuit's holding that *Mobile-Sierra* is inapplicable to third-party challenges. Rather, it argued that *contested settlements* should not be reviewed under the *Mobile-Sierra* standard. See *ibid.* As explained in the petition (at 13 n.4) and below (p. 45, *infra*), this case does not concern the standard that governs FERC's review of a contested settlement. FERC reviewed the settlement here under the ordinary just-and-reasonable standard, not *Mobile-Sierra*. See p. 12, *supra*. This case concerns only the standard that governs *future* challenges to the contract rates produced by the capacity auctions and to the transition payments.

more than 50 years. Just two Terms ago, this Court reaffirmed that bedrock Federal Power Act doctrine, holding that FERC can abrogate contract rates only in "extraordinary circumstances where the public will be severely harmed." *Morgan Stanley Capital Group Inc.* v. *Pub. Util. Dist. No. 1*, 128 S. Ct. 2733, 2749 (2008). In the decision below, the court of appeals created an exception that all but swallows that rule, holding that "the *Mobile-Sierra* doctrine simply does not apply" whenever "a rate challenge is brought by a non-contracting third party." Pet. App. 22a. In the court of appeals' view, *any person* indirectly affected by a contract rate—any consumer, advocacy group, state utility commission, or elected official acting *parens patriae* (indeed, anyone but the contracting parties themselves)—can challenge the rate without regard to *Mobile-Sierra*'s protections.

If the court of appeals were correct, this Court's decision in *Morgan Stanley*—not to mention the half-century of *Mobile-Sierra* jurisprudence that preceded it—would have been an exercise in futility. The Court would have defended the FPA's principle of contract stability by rebuffing the ranks of immediate counterparties only to see the principle overwhelmed by hordes of motivated nonparties lying in wait not far behind. If *Mobile-Sierra*'s demanding public-interest standard protects contracts only from challenges by a select few—the contract counterparties—while exempting everyone else, it provides no stability at all.

But the court of appeals' view is not correct. To the contrary, it cannot be reconciled with this Court's precedents.

A. First, the court of appeals' rationale squarely conflicts with this Court's decision in *Morgan Stanley*. The court of appeals reasoned that applying the public-inter-

est standard to non-parties would "deprive" them of their statutory right to review under the just-and-reasonable standard. But, as *Morgan Stanley* explains, *Mobile-Sierra*'s public-interest standard is merely one "*application* of that just-and-reasonable standard"—the one that governs "contract rates." 128 S. Ct. at 2740. *Mobile-Sierra* "provide[s] a definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context." *Id.* at 2746. The public-interest standard thus cannot "deprive" non-parties of their statutory right to just-and-reasonable review, because it *is* a form of just-and-reasonable review.

B. The public-interest standard, moreover, is a restriction on *FERC's authority* to abrogate contracts, not private parties' authority to challenge them, and it applies whether FERC's investigation is initiated in response to a contracting party's complaint, in response to a non-contracting party's complaint, or by FERC acting *sua sponte*. Indeed, the *public*-interest standard was developed for the precise purpose of protecting the interests of non-contracting members of the *public*. The standard by its terms applies to the public's challenges.

C. Nor can the court of appeals' holding be reconciled with the rationales underlying *Mobile-Sierra*.

1. This Court has premised the *Mobile-Sierra* doctrine on the sensible notion that rates negotiated by sophisticated buyers and sellers can be expected to be reasonable. That expectation of reasonableness cannot logically vary with the identity of the person who challenges the rate. And contract rates agreed to in a competitive wholesale market can be expected to benefit consumers and other non-contracting parties, not just the contracting parties themselves.

2. The court of appeals' decision likewise prevents *Mobile-Sierra* from providing any semblance of the contract stability the doctrine is supposed to provide—stability that is essential to critical infrastructure development. A presumption that protects contract rates from just a few persons (contracting counterparties) while allowing everyone else to challenge them free of *Mobile-Sierra*'s restrictions provides no stability at all.

D. Finally, the court of appeals' decision rests on a misunderstanding of contract principles. Applying *Mobile-Sierra* to a non-party's challenge does not "bind" the non-party to the contract. The existence of the contract is simply a *fact* that makes the rate more likely to be reasonable. And contract-law principles cannot justify making it easier for non-parties to challenge a contract rate, since contract-law principles normally would not allow non-parties to challenge the contract *at all*.

II. A. This Court need not address respondents' alternative argument that, even if *Mobile-Sierra* applies to non-contracting parties as a general matter, the particular rates at issue here are not "contract rates" for *Mobile-Sierra* purposes. This case does not present the question of what standard applies to FERC's review of a proposed *settlement*. FERC reviewed the settlement here under the ordinary just-and-reasonable standard, consistent with the agreement's *Memphis* clause. The agreement's *Mobile-Sierra* provision applies only to *future* challenges to two types of rates: auction rates and transition payments. The Court should leave the question of whether *those* rates are "contract rates" to be addressed, if at all, by the court of appeals in the first instance on remand.

B. In any event, the auction rates are precisely the sort of contract rates that *Mobile-Sierra* has long pro-

tected. Auctions create binding contracts. The auction rates are thus contract rates that would be entitled to *Mobile-Sierra* protection even if there had never been a settlement agreement. FERC could not have erred by approving a settlement provision that merely recites the standard for abrogation that would have applied of its own force even absent the settlement.

ARGUMENT

For more than 50 years, the *Mobile-Sierra* doctrine—named for this Court's twin decisions in *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956) ("*Mobile*"), and *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956) ("*Sierra*")—has "preserv[ed] the integrity of contracts" and thereby "permit[ted] the stability of supply arrangements which all agree is essential to the health of the * * * industry." *Mobile*, 350 U.S. at 344. Under that doctrine, FERC "must presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law," and that "presumption may be overcome only if FERC concludes that the contract seriously harms the public interest." *Morgan Stanley Capital Group Inc.* v. *Pub. Util. Dist. No. 1*, 128 S. Ct. 2733, 2737 (2008).

Mobile-Sierra represents an "application" of the Federal Power Act's general standard that "all wholesale-electricity rates [must] be 'just and reasonable.'" *Morgan Stanley*, 128 S. Ct. at 2737-2740 (quoting 16 U.S.C. §824d(a)) (emphasis omitted). Where a supplier sets a rate unilaterally by tariff, FERC reviews the rate under what is called the "*ordinary* just-and-reasonable standard." See *ibid.* Under that standard, FERC has "discretion to take into account [all] the facts and circumstances" and can select any rate "'within a "zone of reasonableness."'" FERC Pet. Br. 10 (quoting *In re Per-*

mian Basin Area Rate Cases, 390 U.S. 747, 767 (1968)). By contrast, where a buyer and seller agree on a rate by contract, *Mobile-Sierra*'s public-interest standard provides the "definition of what it means for a rate to satisfy the just-and-reasonable standard." *Morgan Stanley*, 128 S. Ct. at 2746. Under the public-interest standard, FERC must "presume" that the contract rate is just and reasonable, and can modify it only in "extraordinary circumstances where the public will be severely harmed." *Id.* at 2737, 2749.

Time and again this Court has confirmed that FERC cannot overturn contract rates unless that public-interest standard is met. In *Mobile*, the Court noted that, "by requiring contracts to be filed with the Commission, the Act expressly recognizes that rates to particular customers may be set by individual contracts," and that the Act "evinces no purpose to abrogate [those] contracts." 350 U.S. at 338. The Commission, the Court concluded, could modify contract rates only "when necessary in the public interest." *Id.* at 344. In *Sierra*, the Court held that "a contract may not be said to be either 'unjust' or 'unreasonable' simply because it is unprofitable to the public utility," and that the "sole concern" of the Commission is whether the contract threatens the "public interest"—such as "where [the rate] might impair the financial ability of the public utility to continue its service, cast upon other consumers an excessive burden, or be unduly discriminatory." 350 U.S. at 355; see also pp. 4-7, *supra* (discussing *Mobile* and *Sierra*). "The regulatory system created by the Act is premised on contractual agreements voluntarily devised by the regulated companies; it contemplates abrogation of these agreements only in circumstances of unequivocal public necessity." *Permian Basin*, 390 U.S. at 822. FERC thus "lacks affirmative

authority, absent extraordinary circumstances, to 'abrogate existing contractual arrangements.'" *Ark. La. Gas Co.* v. *Hall*, 453 U.S. 571, 582 (1981). That "settled understanding of the FPA * * * has prevailed in this Court, lower courts, and the Commission for half a century." *Morgan Stanley*, 128 S. Ct. at 2749 n.6.

Mobile-Sierra reflects the "commonsense notion" that sophisticated businesses in wholesale energy markets can be "'expected to negotiate a "just and reasonable" rate as between the two of them.'" *Morgan Stanley*, 128 S. Ct. at 2746 (quoting *Verizon Commc'ns Inc.* v. *FCC*, 535 U.S. 467, 479 (2002)). (That is why it applies to rates "set bilaterally by contract" but not those set "unilaterally by tariff." See *id.* at 2738.) *Mobile-Sierra* also reflects the need for contractual certainty, a "key source of stability" in volatile energy markets where capital requirements are intensive and cost recovery can take decades. See *id.* at 2749; *Mobile*, 350 U.S. at 344; pp. 40-41, *infra*. As FERC has repeatedly stressed: "Competitive power markets simply cannot attract the capital needed to build adequate generating infrastructure without regulatory certainty, including certainty that the Commission will not modify market-based contracts unless there are *extraordinary* circumstances." *Nev. Power Co.* v. *Duke Energy Trading & Mktg., L.L.C.*, 99 F.E.R.C. ¶61,047, at 61,190 (2002).[5] FERC must presume that

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[5] See also *City of Burbank* v. *Calpine Energy Servs., L.P.*, 102 F.E.R.C. ¶61,268, at 61,832 (2003); *Pub. Util. Dist. No. 1* v. *Am. Elec. Power Serv. Corp.*, 100 F.E.R.C. ¶61,296, at 62,340 (2002); *PacifiCorp* v. *Reliant Energy Servs., Inc.*, 99 F.E.R.C. ¶61,381, at 62,614 (2002); *Pub. Utils. Comm'n of Cal.* v. *Sellers of Long Term Contracts*, 99 F.E.R.C. ¶61,087, at 61,383 (2002). The FERC proceedings in *Nevada Power* and *Public Utilities Commission of California* ultimately led to this Court's rulings in *Morgan Stanley* and related cases.

contract rates are reasonable because "[t]he FPA recognizes that contract stability ultimately benefits consumers." *Morgan Stanley*, 128 S. Ct. at 2749.

In this case, the D.C. Circuit held that, "when a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply." Pet. App. 22a. In other words, although the doctrine protects contract rates from challenges by an immediate counterparty, *any other person* indirectly affected—any consumer, advocacy group, state utility commission, or elected official acting *parens patriae*—can challenge the rate, potentially years into a contract, without regard to *Mobile-Sierra*'s protections. That holding conflicts with this Court's decision in *Morgan Stanley*. It renders the public-interest standard inapplicable to challenges by the very members of the public the doctrine is designed to protect. It makes the presumption of reasonableness vary with the challenger, despite the fact that this Court's rationales for presuming reasonableness do not depend on the identity of the complainant who prompted FERC's investigation. It destroys the contract stability that *Mobile-Sierra* was designed to provide. And it rests on a fundamentally mistaken conception of contract law.

I. *MOBILE-SIERRA* REQUIRES FERC TO PRESUME THAT CONTRACT RATES ARE REASONABLE REGARDLESS OF THE CHALLENGER'S IDENTITY

A. *Morgan Stanley* Squarely Rejected the Court of Appeals' Rationale for Limiting *Mobile-Sierra* to Challenges by Contracting Parties

The court below held that, "when a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply; the proper standard of review remains the 'just and reasonable' standard in section 206 of the Federal Power Act." Pet. App. 22a.

That holding rested entirely on the premise that *Mobile-Sierra*'s public-interest test is inconsistent with the statutory "just and reasonable" standard. "[T]he relevant statutory language," the court noted, "is quite clear": FERC "must determine whether the challenged rate is 'unjust, unreasonable, unduly discriminatory or preferential.'" Pet. App. 23a-24a (quoting 16 U.S.C. §824e(a)). The court acknowledged *Mobile-Sierra*'s public-interest standard, but characterized *Mobile-Sierra* as having "carve[d] out an exception" to the statutory just-and-reasonable requirement "based on the 'familiar dictates of contract law.'" *Id.* at 20a. Because "'a contract cannot bind a nonparty,'" the court reasoned, the public-interest standard cannot be "thrust" upon non-contracting third parties. *Id.* at 22a (quoting *EEOC* v. *Waffle House, Inc.*, 534 U.S. 279, 294 (2002)). Doing so would "deprive them of their statutory right to challenge rates under the 'just and reasonable' standard." *Id.* at 19a.

Over and over the court of appeals made that same point. The public-interest standard would "deprive[] non-settling parties of their statutory right to have rate challenges adjudicated under the 'just and reasonable' standard." Pet. App. 22a. It would "derogat[e] [from] the[ir] statutory right to 'just and reasonable' review." *Id.* at 23a n.9. It "departs from the usual 'just and reasonable' standard and makes it harder for petitioners to successfully challenge rates in cases of changed circumstances." *Id.* at 23a. FERC cannot even apply *Mobile-Sierra* narrowly to discrete issues where stability is critical, the court declared, because doing so would be tantamount to "us[ing] an illegal standard sparingly." *Ibid.*

That reasoning cannot be reconciled with this Court's decision in *Morgan Stanley*. There, this Court flatly rejected the view that *Mobile-Sierra*'s public-interest stan-

dard departs from the statutory "just and reasonable" standard. The Court acknowledged that FERC and courts had begun to refer to the standard governing unilateral tariff rates as the "just and reasonable standard" and *Mobile-Sierra*'s standard for contract rates as the "public interest standard." 128 S. Ct. at 2740. But the Court rejected as "obviously indefensible" the claim that "a standard different from the statutory just-and-reasonable standard applies to contract rates." *Ibid.* "Rather, the term 'public interest standard' refers to the differing *application* of that just-and-reasonable standard to contract rates." *Ibid.* *Mobile-Sierra*'s public-interest standard simply "provide[s] a definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context." *Id.* at 2746.

The decision below thus adopted the very position this Court rejected in *Morgan Stanley*: that the public-interest standard "departs" from or is an "exception" to the Act's requirement that all rates be "just and reasonable." Applying *Mobile-Sierra* to non-party challenges cannot "deprive [non-parties] of their statutory right to challenge rates under the 'just and reasonable' standard," Pet. App. 19a, because *Mobile-Sierra*'s public-interest standard is simply an *application* of that statutory standard—the "definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context." *Morgan Stanley*, 128 S. Ct. at 2746. Because the decision below rests on a premise this Court has squarely rejected, it should be reversed.

B. The Court of Appeals' Analysis Cannot Be Reconciled with the Requirement That FERC Apply the Public-Interest Standard to Address Third-Party Harm

The court of appeals' claim that *Mobile-Sierra* does not apply to challenges by non-contracting third parties also defies the settled framework under which FERC must address third-party harm. *Mobile-Sierra* limits *FERC's authority* to abrogate contract rates. And, under *Mobile-Sierra*'s public-interest standard, whether FERC can abrogate a contract rate depends on whether there is harm to the public interest, not on the identity of the party that filed the complaint. *Mobile-Sierra*'s "public interest" standard exists for the precise purpose of protecting the "public"—*i.e.*, non-contracting third parties. The court of appeals' holding stands *Mobile-Sierra* on its head, rendering the public-interest standard inapplicable to challenges by the very parties it was designed to protect.

1. *Mobile-Sierra*'s "public interest" standard exists to protect the interests of non-contracting third parties. Indeed, that is its *sole* purpose. In *Mobile*, the Court stated that its interpretation "preclud[ed] [suppliers] from unilaterally changing their contracts simply because it is in their *private* interests to do so." 350 U.S. at 344 (emphasis added). The *only* situation where suppliers would have an "avenue of relief," the Court explained, was where their "private interests" happened to "coincide with the public interest." *Ibid.* *Mobile* thus conditioned relief on harm to the *public*—*i.e.*, to non-contracting third parties—as opposed to the "private interests" of the contracting parties.

Sierra underscores that point. The "purpose of the power given the Commission by § 206(a)," the Court

stated, "is the protection of the public interest, *as distinguished from the private interests of the utilities.*" 350 U.S. at 355 (emphasis added). The "*sole concern* of the Commission" in contract cases is "whether the rate * * * adversely affect[s] the *public* interest." *Ibid.* (emphasis added). The Court then gave three examples of that "public" harm—"where [the rate] might impair the financial ability of the public utility to continue its service, cast upon other consumers an excessive burden, or be unduly discriminatory." *Ibid.* Each of those examples concerns harm to non-contracting third parties. The prospect that a utility might be unable to "continue its service" portends serious harm to the consuming public, which might find itself without electricity. Cf. *Blumenthal* v. *NRG Power Mktg., Inc.*, 104 F.E.R.C. ¶61,210, at 61,731 (2003) (refusing to abrogate a contract that would not "impair or interrupt the reliability of electric service to end users"). The prospect of casting an "excessive burden" on "*other* consumers" by its terms involves third-party harms. And "unduly discriminatory" rates concern third-party harms too, as that phrase refers only to rates that are "unduly discriminatory or preferential to the detriment of purchasers *who are not parties to the contract.*" *Papago Tribal Util. Auth.* v. *FERC*, 723 F.2d 950, 953 n.4 (D.C. Cir. 1983) (Scalia, J.) (emphasis added); see also *Ne. Utils. Serv. Co.* v. *FERC*, 993 F.2d 937, 960-961 (1st Cir. 1993).

Later cases have elaborated on the *degree* of harm that *Mobile-Sierra* requires. See pp. 21-23, *supra*. But the relevant harm has always been harm *to the public*—*i.e.*, to third parties. See, *e.g.*, *Morgan Stanley*, 128 S. Ct. at 2747 (harm to "customers of the purchaser"); *Potomac Elec. Power Co.* v. *FERC*, 210 F.3d 403, 406-410 (D.C. Cir. 2000); *Pub. Serv. Comm'n* v. *FPC*, 543 F.2d 757, 796-

798 (D.C. Cir. 1974). "The focus of the *Mobile-Sierra* doctrine has always been on the impact * * * on third parties * * *." *Blumenthal*, 104 F.E.R.C. ¶61,210, at 61,730.

2. This Court's cases, the statutory text, and decades of precedent make clear that the D.C. Circuit's approach—ignoring the "public interest" standard whenever the challenger is a member of the public—is wrong. *Mobile-Sierra*'s public-interest test defines *FERC's authority* to abrogate contract rates. And that authority depends on the extent of injury to the public—not on the identity of the complainant who prompted FERC's investigation.

This Court has consistently described *Mobile-Sierra*, not as a limit on *private parties'* ability to challenge contract rates, but as a restriction on *FERC's* authority to modify rates. Every reference in *Morgan Stanley* describes the doctrine in those terms: "Under the *Mobile-Sierra* doctrine, *the Federal Energy Regulatory Commission* * * * *must presume* that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law." 128 S. Ct. at 2737 (emphasis added). *Mobile* and *Sierra* "addressed the *authority of the Commission* to modify rates set bilaterally by contract." *Id.* at 2738 (emphasis added). "[T]he FPA intended to reserve *the Commission's* contract-abrogation power for those extraordinary circumstances where the public will be severely harmed." *Id.* at 2749 (emphasis added). As the Court stated elsewhere: "[T]he *Commission itself* lacks affirmative authority, absent extraordinary circumstances, to 'abrogate existing contractual arrangements.'" *Ark. La.*, 453 U.S. at 582 (emphasis added). FERC likewise understands *Mobile-Sierra* as a restriction on *its own* authority—a

doctrine that creates necessary certainty by prohibiting "*the Commission* [from] modify[ing] market-based contracts unless there are extraordinary circumstances." *Nev. Power*, 99 F.E.R.C. ¶61,047, at 61,190 (emphasis altered). Because *Mobile-Sierra* restricts FERC, not private parties, the complainant's identity is immaterial. Anyone aggrieved can file a complaint. *Mobile-Sierra* simply restricts FERC's authority to abrogate contracts in response.

The statutory text confirms that understanding. The statute charges *FERC* with determining whether rates are just and reasonable. 16 U.S.C. §§824d(e), 824e(a). "[T]he prescription of the statute is a standard for the Commission to apply and, independently of Commission action, creates no right which courts may enforce." *Montana-Dakota Utils. Co.* v. *Nw. Pub. Serv. Co.*, 341 U.S. 246, 251 (1951). FERC can initiate proceedings "upon its own motion or upon complaint," 16 U.S.C. §824e(a), but nothing in the statute suggests that FERC's authority depends on how the investigation began. As FERC explained below, it would be "manifestly anomalous" to make "the Commission's ability to change an agreement * * * vary based on whether a third party filed a complaint, instead of the extent to which third parties are harmed by that agreement." FERC Reh'g Pet. in Nos. 06-1403 *et al.*, at 11 (D.C. Cir. Aug. 8, 2008). One of the sources on which the court below relied (Pet. App. 20a n.8) makes that very point: "While a substantive finding at the conclusion of a proceeding that third parties' interests are at stake and are damaged could be a legitimate factor * * *, the manner of initiating the investigation—*sua sponte* or at the request of a non-contracting party versus at the request of a contracting party—should have no bearing on the final Commission order." Gentile, *The*

Mobile-Sierra *Rule: Its Illustrious Past and Uncertain Future*, 21 Energy L.J. 353, 371 (2000). "Section 206 of the FPA * * * do[es] not vest the Commission with different authorities based on the manner in which an investigation is initiated." *Ibid.*

Lower courts have long applied *Mobile-Sierra* without regard to the challenger's identity. In *Northeast Utilities Service Co.* v. *FERC*, 993 F.2d 937 (1st Cir. 1993), for example, a non-party disputed the reasonableness of certain contract terms. See *Ne. Utils. Serv. Co.*, 50 F.E.R.C. ¶61,266, at 61,831-32, 61,837-39 (1990). FERC stated that, because "parties to a contract can[not] waive the section 206 rights of nonparties," "a nonparty challeng-[ing] a rate contract in a section 206 proceeding * * * need only show that the contract is unjust, unreasonable, unduly discriminatory or preferential." *Id.* at 61,838. The First Circuit reversed. It acknowledged FERC's concern that the contract "might unduly discriminate against entities not parties to the contract." 993 F.2d at 961. But that concern was "inadequate" to justify departure from *Mobile-Sierra* because "[t]he *Mobile-Sierra* doctrine itself allows for intervention by FERC where it is shown that the interests of third parties are threatened." *Ibid.* Harm to third parties, the court held, was not a "reason for departing from this public interest standard." *Ibid.* When FERC modified the contract again on remand, the First Circuit affirmed because FERC properly "applied the 'public interest' doctrine," "explaining how the disputed contractual terms may harm third parties." *Ne. Utils. Serv. Co.* v. *FERC*, 55 F.3d 686, 692-693 (1st Cir. 1995). Other cases are to the same effect.[6] And FERC itself has routinely applied *Mo-*

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[6] In *Wisconsin Public Power, Inc.* v. *FERC*, 493 F.3d 239 (D.C. Cir. 2007), for example, the D.C. Circuit applied *Mobile-Sierra* despite

bile-Sierra to non-party challenges.[7]

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non-parties' arguments that the contracts would "shift congestion costs to everyone else in the market." *Id.* at 273-275. And in *Town of Norwood* v. *FERC*, 587 F.2d 1306 (D.C. Cir. 1978), the court applied *Mobile-Sierra* to a *non-party's* complaint of undue discrimination, stating that FERC could modify a contract as a remedy only if the "heavy burdens" of *Mobile Sierra* were met. *Id.* at 1312.

[7] See *Midwest Indep. Sys. Operator, Inc.*, 115 F.E.R.C. ¶61,174, at 61,615 (2006); *Vt. Elec. Coop., Inc.*, 114 F.E.R.C. ¶61,220, at 61,715 (2006); *Calpine Constr. Fin. Co.*, 114 F.E.R.C. ¶61,217, at 61,711 (2006); *Hermiston Power P'ship*, 114 F.E.R.C. ¶61,204, at 61,689 (2006); *San Diego Gas & Elec. Co.*, 114 F.E.R.C. ¶61,158, at 61,521 (2006); *Midwest Indep. Sys. Operator, Inc.*, 110 F.E.R.C. ¶61,380, at 62,469-70 (2005); *Midwest Indep. Sys. Operator, Inc.*, 110 F.E.R.C. ¶61,177, at 61,653-54 (2005); *Wis. Power & Light Co.*, 106 F.E.R.C. ¶61,112, at 61,410-11 (2004); *PJM Interconnection*, 105 F.E.R.C. ¶61,294, at 62,427, 62,430 (2003), *reh'g denied*, 108 F.E.R.C. ¶61,032, at 61,204 (2004); *Pub. Utils. Comm'n of Cal.* v. *Sellers of Long Term Contracts*, 105 F.E.R.C. ¶61,182, at 61,947 (2003); *Nev. Power Co.* v. *Enron Power Mktg., Inc.*, 103 F.E.R.C. ¶61,353, at 62,389 (2003), *reh'g denied*, 105 F.E.R.C. ¶61,185, at 61,985 (2003); cf. *Cent. Me. Power Co.*, 114 F.E.R.C. ¶61,184, at 61,621 (2006); *Pub. Utils. Comm'n of Cal.* v. *Sellers of Long Term Contracts*, 99 F.E.R.C. ¶61,087 at 61,382-83 (2002), *reh'g denied*, 100 F.E.R.C. ¶61,098, at 61,395-96 (2002).

Admittedly, FERC has sometimes declined to apply the public-interest standard to non-parties. See, *e.g.*, *Bridgeport Energy, LLC*, 118 F.E.R.C. ¶61,243, at 62,193-94 (2007); *PJM Interconnection, LLC*, 96 F.E.R.C. ¶61,206, at 61,878 & n.13 (2001); *Fla. Power & Light Co.*, 67 F.E.R.C. ¶61,141, at 61,394-99 (1994); *So. Co. Servs., Inc.*, 67 F.E.R.C. ¶61,080, at 61,226-29 (1994). But many of those decisions rest on special circumstances or the absence of FERC consent and thus do not support the categorical rule adopted below. In any event, FERC's sometimes overt hostility to *Mobile-Sierra*—a doctrine that constrains its discretion—is well documented. See, *e.g.*, *Boston Edison Co.* v. *FERC*, 233 F.3d 60, 67-68 (1st Cir. 2000) (FERC is "becoming hostile to *Mobile-Sierra*" and will "say anything it needs to achieve its ends"); *Richmond Power & Light* v. *FPC*, 481 F.2d 490, 497 (D.C. Cir. 1973) ("[T]he Commission simply does not understand, or more likely is not willing to abide by," *Mo-*

This Court's decision in *Mobile* compels that result. In that case, the relevant provision of the Natural Gas Act (unlike its FPA counterpart) did not give suppliers standing to file complaints. See 350 U.S. at 344-345; compare 15 U.S.C. §717d(a) with 16 U.S.C. §824e(a). The Court recognized that, as a result, a natural gas supplier's *only* "avenue of relief" was to "furnish[ ] to the Commission any relevant information and request[ ] *it* to initiate an investigation *on its own motion*" in the hope that the supplier's interests would "coincide with the public interest." 350 U.S. at 344-345 (emphasis added). *Mobile* thus demonstrates that the public-interest standard applies even when FERC initiates a proceeding itself. See also *Boston Edison Co.* v. *FERC*, 233 F.3d 60 (1st Cir. 2000).

The D.C. Circuit's holding that *Mobile-Sierra* applies *only* to challenges by *contracting* parties cannot be reconciled with *Mobile*'s conclusion that the doctrine applies to challenges FERC initiates itself. FERC, after all, is the quintessential non-contracting party. Nor does it make any sense that FERC, the federal regulator statutorily charged with protecting the public interest, would have to meet *Mobile-Sierra*'s demanding public-interest standard while state attorneys general, advocacy groups, and litigious third parties—which lack FERC's expertise and statutory authority—can challenge those same rates free of *Mobile-Sierra*'s restrictions. The simple fact is that *Mobile-Sierra*'s public-interest standard applies *whenever* FERC considers abrogating a contract—whether in response to a contracting party's complaint, in response to a non-contracting party's complaint, or on its own motion.

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bile-Sierra); *Sam Rayburn Dam Elec. Coop.* v. *FPC*, 515 F.2d 998, 1005 & n.29 (D.C. Cir. 1975); *Borough of Lansdale* v. *FPC*, 494 F.2d 1104, 1110 (D.C. Cir. 1974).

C. The Court of Appeals' Decision Cannot Be Reconciled With *Mobile-Sierra*'s Underlying Rationales

The court of appeals' categorical exemption for non-party challenges also contravenes the rationales underlying *Mobile-Sierra*. Those rationales are implicated whenever FERC contemplates abrogating a contract, without regard to the complainant's identity.

1. *This Court's Conclusion That Contract Rates Can Be Expected To Be Reasonable Applies Regardless of Who Challenges the Rates*

This Court has repeatedly grounded *Mobile-Sierra* in the sensible notion that a rate agreed upon by a buyer and seller—as opposed to a tariff dictated unilaterally by the seller—can be expected to be reasonable. *Mobile-Sierra* reflects "the commonsense notion that '[i]n wholesale markets, the party charging the rate and the party charged [are] often sophisticated businesses enjoying presumptively equal bargaining power, who could be expected to negotiate a "just and reasonable" rate as between the two of them.'" *Morgan Stanley*, 128 S. Ct. at 2746 (quoting *Verizon*, 535 U.S. at 479). That is why FERC must "presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law." *Id.* at 2737.

That expectation—that a contract rate will generally be reasonable—logically cannot depend on the identity of the person who challenges it. Contract rates can affect a variety of persons, both contracting parties and non-parties. But the identities of the persons affected, and the magnitude of those effects, do not depend on how FERC's investigation begins. A reasonable effect on the public cannot be transformed into a serious harm to the public, or vice versa, based on who filed the complaint.

As a matter of logic, the presumption of reasonableness "would not necessarily cease to apply simply because the challenge to the rate came from a non-contracting party." FERC Pet. Br. 14.

Moreover, contract rates negotiated by sophisticated parties can be expected to be reasonable even insofar as they affect third parties. That basic economic principle underlies FERC's entire "market-based rate" regime. See *Morgan Stanley*, 128 S. Ct. at 2741 (describing regime). Courts have upheld that regime precisely because rates freely negotiated in a competitive market are likely to be "just and reasonable"—not in the narrow sense that the parties get what they bargained for, but in the broader sense of economic efficiency. "'In a competitive market, * * * it is rational to assume that the terms of [the parties'] voluntary exchange are reasonable, and specifically to infer that the price is close to marginal cost, such that the seller makes only a normal return on its investment.'" *Elizabethtown Gas Co.* v. *FERC*, 10 F.3d 866, 870-871 (D.C. Cir. 1993) (quoting *Tejas Power Corp.* v. *FERC*, 908 F.2d 998, 1004 (D.C. Cir. 1990)); *California ex rel. Lockyer* v. *FERC*, 383 F.3d 1006, 1012-1013 (9th Cir. 2004); see also *Market-Based Rates*, 72 Fed. Reg. 39,904, 40,015-20 (2007).[8] Whether a rate is "close to marginal cost" and yields "only a normal return" in the long run cannot depend on the identity of the person affected. The presumption that market-based rates are reasonable thus is entirely independent of the challenger's identity. The *Mobile-Sierra* presumption must be as well.

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[8] Of course, the fact that market prices can be expected to approximate marginal costs *in the long run* does not mean that merely exceeding marginal cost in a particular case overcomes the presumption of reasonableness. See *Morgan Stanley*, 128 S. Ct. at 2748-2749 & n.5.

The D.C. Circuit made no effort to explain why the expectation that contract rates will be reasonable should depend on who challenges them. Although the court alluded to the "superior efficiency of private bargaining," Pet. App. 19a, it never explained why that "superior efficiency" disappears when the presumptively efficient results of that bargaining are challenged by a non-contracting party. Respondents invoke *Morgan Stanley*'s observation that sophisticated parties could be "'expected to negotiate a "just and reasonable" rate *as between the two of them*.'" Br. in Opp. 15 (quoting 128 S. Ct. at 2746 (emphasis added)). But respondents misinterpret the phrase "as between the two of them." The Court's point was simply that a rate that is "just and reasonable" for two parties engaged in one transaction would not necessarily be "just and reasonable" for a different transaction involving different parties. Nothing in that phrase implies that the presumption of reasonableness evaporates when a rate is challenged by a non-party.

There may be unusual situations where a contract, although satisfactory to the contracting parties, imposes excessive or discriminatory burdens on third parties. But that proves only that FERC must have authority to abrogate contracts that sufficiently *affect* third parties, not that FERC's authority should depend on the identity of the complainant who caused FERC to initiate its investigation. And the public-interest standard already provides the proper mechanism for FERC's exercise of that authority: It permits FERC to abrogate contracts that "seriously harm[]" the public interest. *Morgan Stanley*, 128 S. Ct. at 2737. No one claims the presumption of reasonableness should be irrebuttable. The question is only whether the basis for the presumption evapo-

rates simply because a non-contracting party challenges the rate. Clearly it does not.

2. *Challenges to Contracts Threaten Stability Regardless of the Challenger's Identity*

This Court has also grounded *Mobile-Sierra* in the "important role" contracts play in the FPA by providing a "key source of stability" that "ultimately benefits consumers." *Morgan Stanley*, 128 S. Ct. at 2749. Contracting parties often must undertake "substantial investments which [they] would be unwilling to make without long-term commitments," and parties can "hardly make such commitments if [their] supply contracts are subject to unilateral change * * * whenever [the other party's] interests so dictate." *Mobile*, 350 U.S. at 344; see pp. 7-8, 23-24, *supra*. This Court could not have held that *Mobile-Sierra* promotes contract stability if the doctrine applied only to challenges by contracting parties. A presumption that protects contracts from only a few people—the counterparties—while allowing *everyone else* to challenge them without regard to *Mobile-Sierra*'s protections provides no stability at all.

Wholesale energy contracts indirectly affect a vast array of consumers and other entities. Under the broad principles of administrative-law standing, virtually any of those indirectly affected persons can file a complaint. The FPA authorizes "*[a]ny person*, electric utility, State, municipality, or State commission" to complain. 16 U.S.C. § 825e (emphasis added). FERC regulations similarly permit "*[a]ny person* [to] file a complaint seeking Commission action." 18 C.F.R. § 385.206(a) (emphasis added). And even an "'identifiable trifle'" may confer standing. *United States* v. *SCRAP*, 412 U.S. 669, 689 n.14 (1973). Thus, the field of potential complainants is vast. It includes not only the contracting parties, but

thousands of retail electricity consumers or other downstream purchasers; any interest group with a perceived stake (whether it seeks lower prices to benefit consumers or higher ones to promote conservation); and any state utility commission, consumer advocate, or elected official acting *parens patriae*.

One need look no further than *Morgan Stanley* to see the impact of the court of appeals' holding. In that case, this Court overturned the Ninth Circuit's refusal to apply the public-interest standard. 128 S. Ct. at 2745-2747. But myriad non-contracting parties (including the Nevada Public Utilities Commission, various Snohomish County ratepayers, and a U.S. Senator) had challenged the contracts in the underlying FERC proceedings,[9] and one non-contracting party (the Office of Nevada Attorney General, Bureau of Consumer Protection) was a respondent in this Court, see Br. for Pub. Util. Dist. No. 1, Nevada BCP, *et al.*, in Nos. 06-1457 & 06-1462, at 20 (Jan. 7, 2008). On the D.C. Circuit's theory, *Morgan-Stanley* should have come out the other way.

In this case too, nearly all the objectors are at most indirectly affected. See Pet. App. 120a-121a & nn.31-32, 144a. They include a "non-profit trade association" representing "industrial users of electricity," Br. in Opp. ii; an "ad hoc association of large industrial and commercial end-users," *id.* at iii; a consortium with such members as Brandeis University and the Polaroid Corporation, see Pet. App. 121a n.32; the attorneys general of two States, *ibid.*; one public utilities commission, *id.* at 121a n.31; and one public advocate, *ibid.* The Connecticut Attorney General asserts that *Mobile-Sierra* should not apply to

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[9] See *Nev. Power*, 103 F.E.R.C. ¶61,353, at 62,388-89; *Nev. Power*, 105 F.E.R.C. ¶61,185, at 61,985; see also *Pub. Utils. Comm'n of Cal.*, 99 F.E.R.C. ¶61,087, at 61,377, 61,382-83.

him even though that State's utility regulator (the Department of Public Utility Control) and utility ratepayer advocate (the Office of Consumer Counsel) both *supported* the settlement. See J.A. 89. Other examples of non-party challenges abound.[10]

It is thus no surprise that those who actually negotiate wholesale contracts see non-party challenges as a threat to contract stability. In the first 12 months following the decision below, FERC had to rewrite contracts applying the *Mobile-Sierra* standard to non-parties at least 41 times. See Pet. Reply App. 1a-10a. That so many thought it desirable to include such provisions confirms that non-party challenges are a real threat. Exempting *every* challenger from *Mobile-Sierra* except an isolated few—the contract counterparties themselves—would destroy the stability the doctrine was designed to promote.

The court of appeals asserted that "[i]t makes no sense to say that the values of 'stability' and 'certainty' are furthered by applying the deferential standard of review to * * * parties that refused to agree." Pet. App. 24a (emphasis omitted). Quite the opposite: It "makes no sense" to justify *Mobile-Sierra* on the need to ensure contract stability but then to exempt challenges by a vast field of potential complainants with powerful incentives to upset

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[10] The Illinois Attorney General recently challenged contracts between 16 wholesale suppliers and utilities, and won a settlement. See *Illinois ex rel. Ill. Att'y Gen.* v. *Exelon Generation Co.*, 121 F.E.R.C. ¶61,015 (2007). And a California consumer interest group—CAlifornians for Renewable Energy, Inc., or "CARE"—challenged several contracts between suppliers and utilities. See *CAlifornians for Renewable Energy, Inc.* v. *Cal. Pub. Utils. Comm'n*, 119 F.E.R.C. ¶61,058 (2007) (dismissing complaints); *CAlifornians for Renewable Energy, Inc.* v. *Cal. Pub. Utils. Comm'n*, 120 F.E.R.C. ¶61,272 (2007) (same). Some of those challenges remain pending on appeal. See No. 08-70010 (9th Cir. filed Jan. 3, 2008).

the agreements. From the perspective of power suppliers, it makes no difference whether their contracts are abrogated—potentially years into a project—because their counterparties complained or because someone else did. Stability is destroyed either way. The D.C. Circuit's decision would thus reduce *Mobile-Sierra*'s role in ensuring contract stability to a historical footnote.

That result could not come at a worse time. Over the next two decades, demand for electricity is expected to grow substantially, requiring some $400 to $700 billion in additional infrastructure. See The Brattle Group, *Transforming America's Power Industry: The Investment Challenge 2010-2030*, at 13, 20-21 (2008), http://www.edisonfoundation.net. But building a power plant typically takes years, and recovering its costs takes many more. See Cambridge Energy Research Assocs., Inc., *California Power Crisis Aftershock: The Potential Modification of Western Power Contracts* 4-5 (2007), http://www2.cera.com/westernpowercontracts. Electricity prices, moreover, are notoriously volatile. See *id.* at 7-9. Without reliable long-term contracts to assure predictable revenue streams, infrastructure developers would face enormous risks, requiring them either to pay substantial risk premiums for financing (costs that are ultimately passed on to consumers) or to abandon development altogether. See *id.* at 4-26. As FERC has explained, "[c]ompetitive power markets simply cannot attract the capital needed to build adequate generating infrastructure without regulatory certainty, including certainty that the Commission will not modify market-based contracts unless there are *extraordinary* circumstances." *Nev. Power*, 99 F.E.R.C. ¶61,047, at 61,190. Contract stability, moreover, is particularly important for renewable energy resources. See Cambridge Energy Research Assocs., *su-*

pra, at 19. The impending federal renewable-energy requirements thus make *Mobile-Sierra* even more crucial. See American Clean Energy and Security Act of 2009, H.R. 2454, 111th Cong., § 101.

The point is not that *Mobile-Sierra should* apply to third-party challenges because contract stability is good policy. The point is that *Mobile-Sierra must* apply to third-party challenges because the court of appeals' contrary rule makes nonsense of this Court's stated rationale for the doctrine. A presumption of reasonableness that governs challenges by a select few—counterparties—but exempts challenges by everyone else, including consumers, interest groups, elected officials, or any other member of the essentially boundless class of indirectly affected non-parties, simply cannot provide the "stability of supply arrangements which all agree is essential to the health of the * * * industry." *Mobile*, 350 U.S. at 344.

D. The Court of Appeals' Decision Rests on an Erroneous Understanding of Contract Law

The court of appeals' decision also rests on a mistaken understanding of contract law. The court exempted everyone but contract signatories from *Mobile-Sierra* on the theory that a contract "binds" contracting parties to the public-interest standard but cannot "bind" non-parties. "'[I]t goes without saying,'" the court reasoned, "'that a contract cannot bind a nonparty.'" Pet. App. 22a (quoting *Waffle House*, 534 U.S. at 294).

A contract, however, does not "bind" a non-party merely because its existence somehow *affects* that non-party. Every moviegoer, for example, is indirectly affected by dozens of contracts to which the theater owner is a party—the license agreement with the studio that provided the film, the employment contract with the projectionist, even the contract with the popcorn supplier.

But no one would say the moviegoer is "bound" by those contracts. This Court confirmed that common-sense principle in *Local No. 93, International Association of Firefighters* v. *City of Cleveland*, 478 U.S. 501 (1986), concluding that a union was not "b[ou]nd" by a settlement agreement to which it was not a party, even though the union claimed the agreement affected it by diminishing workforce competence. See *id.* at 507-512, 528-530. What mattered, the Court explained, was that the agreement "impose[d] no legal duties or obligations on the Union" and "d[id] not purport to resolve any claims the Union might have." *Id.* at 530.

Wholesale power contracts are no different. A utility's retail customers, for example, are not "bound" by the wholesale contracts between the utility and its power suppliers. Consumers have no rights or obligations under those contracts; they normally are not even third-party beneficiaries. Cf. 13 R. Lord, *Williston on Contracts* §37:34, at 219 (4th ed. 2000). The wholesale contract rate may indirectly *affect* retail consumers by affecting the utility's costs and thus its retail rates. But that does not mean consumers are "bound" by the contract.

The same principle governs FERC's standard of review. Under *Mobile-Sierra*, the existence of a contract *affects* the standard that FERC must apply when it reviews a rate. It thus *affects* non-contracting parties' ability to obtain modification of the rate. But the contract does not *bind* either FERC or non-parties by its own legal force. The existence of the contract is simply a *fact* that makes the rate more likely to be just and reasonable. *Mobile-Sierra* requires FERC to presume that contract rates are just and reasonable because sophisticated wholesale market participants can be expected to negoti-

ate reasonable rates and because the FPA recognizes that contract stability ultimately benefits consumers—not because FERC or non-parties are contractually "bound" to that standard. See pp. 34-41, *supra*.

For that reason, the court of appeals erred in relying on *Waffle House*'s observation that a contract cannot "bind" non-parties. Pet. App. 22a. The question in *Waffle House* was whether an employee's agreement to arbitrate barred the EEOC from seeking judicial relief for him. 534 U.S. at 282. The contract was potentially relevant only on the theory (rejected by the Court) that the agreement *bound* the EEOC *by its legal force* not to pursue judicial relief. See *id.* at 284, 294. *Mobile-Sierra*, by contrast, does not rest on the theory that a wholesale energy contract "binds" FERC or the public *by its own legal force*. The existence of the contract is simply a *fact* that makes the rate presumptively just and reasonable.

To the extent general contract-law principles are relevant, they cut *against* the court of appeals' decision. Contract law generally does not allow non-parties to challenge contracts between others. "Ordinarily, only a party * * * to a contract can challenge its validity," and "the fact that a third party would be better off if a contract were unenforceable does not give him standing to sue to void the contract." *In re Vic Supply Co.*, 227 F.3d 928, 930-931 (7th Cir. 2000) (Posner, J.); see also *Ope Shipping, Ltd.* v. *Allstate Ins. Co.*, 687 F.2d 639 (2d Cir. 1982) ("Where, as here, the parties to a [contract] are satisfied with their bargain, a third person * * * may not challenge the contract's validity * * * ."); cf. *Friend* v. *Lee*, 221 F.2d 96, 100 (D.C. Cir. 1955) (non-party "has no standing to sue to invalidate the contract"). Contract law, for example, gives shoppers no right to challenge the rate the local grocer agrees to pay a farmer for lettuce, even if that

agreement affects the grocer's prices. Likewise, contract law would not itself allow consumers to challenge the rate a utility pays for capacity merely because that rate affects their electricity bills.

The FPA departs from contract-law principles by adopting the broad standing principles of administrative law and by authorizing FERC to abrogate contracts that seriously harm third parties' interests. See pp. 27-29, 37, *supra*. But contract law cannot justify a further expansion of FERC's authority based on the challenger's identity. One cannot invoke general contract-law principles to expand a non-party's ability to challenge a rate where those contract-law principles would not permit him to bring the challenge *at all*.

Ultimately, the court of appeals seems to have treated *Mobile-Sierra* as a contractual waiver or estoppel doctrine. The court seems to have reasoned that, when parties enter into a contract, they impliedly waive their own right to just-and-reasonable review—a waiver that cannot be thrust upon third parties without depriving them of their separate right to just-and-reasonable review. See Pet. App. 19a-24a. Even apart from that theory's patent conflict with *Morgan Stanley*, see pp. 24-26, *supra*, this Court has never justified *Mobile-Sierra* on waiver or estoppel grounds. The Court's actual rationales for presuming contract rates to be reasonable—that sophisticated parties can be expected to negotiate reasonable rates and that contract stability benefits consumers—do not depend on the challenger's identity. See pp. 34-41, *supra*.

In *Morgan Stanley*, this Court rejected a similar attempt to reconceptualize *Mobile-Sierra* and then narrow the doctrine's scope based on the reconceived rationale. There, the Ninth Circuit had treated *Mobile-Sierra* as an

"estoppel" doctrine that applied only after FERC's initial opportunity for review. See 128 S. Ct. at 2745-2746. This Court rejected that estoppel theory, pointing out that its cases had "said nothing of the sort." *Id.* at 2746. The court of appeals' theory here is equally unsupported by precedent. And it is at least as destructive of the goals *Mobile-Sierra* is designed to serve.

II. The Court Need Not Address—And In Any Event Would Have To Reject—Respondents' Alternative Ground For Affirmance

A. This Court Need Not Address Respondents' Alternative Argument

In their brief in opposition, respondents urged that *Mobile-Sierra* should not apply here because the agreements at issue are "fundamentally different from the privately negotiated bilateral energy contracts that were at issue in *Morgan Stanley*." Br. in Opp. 10-12. To the extent respondents contend that *Mobile-Sierra* cannot apply to FERC's review of a *settlement agreement* (*id.* at 10), this case does not present that issue. FERC reviewed the settlement under the ordinary just-and-reasonable standard, consistent with the agreement's *Memphis* clause. See pp. 11-12, *supra*. *Mobile-Sierra* governs only *future* challenges in two narrow contexts excepted from that *Memphis* clause—rates agreed upon through the auctions, and transition payments. See *ibid.* Nor does this case concern whether FERC could have required, as a condition to approving the settlement, an even broader *Memphis* clause that would have withheld *Mobile-Sierra* protection from those two categories of rates as well. FERC approved the settlement, including its *Mobile-Sierra* provision, after concluding that the agreement appropriately balances all competing interests. See Pet. App. 202a.

Respondents' argument thus reduces to the assertion that auction rates and transition payments are not "contract rates" entitled to *Mobile-Sierra* protection. This Court, however, need not and should not resolve that quite distinct issue (which was presented as a separate argument both before FERC, see p. 14, *supra*, and by intervenors in the court of appeals, see Joint Intervenors' Br. in Nos. 06-1403 *et al.*, at 16-28 (D.C. Cir. Sept. 5, 2007)). The court of appeals did not address that issue. Instead, the court based its decision on the identity of the complaining party: "[W]hen a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply * * * ." Pet. App. 22a. The correctness of that categorical holding is the only question presented by the petition. Pet. i. And that is the only question of broad and recurring importance that has divided the courts of appeals. See *id.* at 25-28.

This Court's normal practice is "not [to] decide in the first instance issues not decided below." *NCAA* v. *Smith*, 525 U.S. 459, 469-470 (1999); see also *Muehler* v. *Mena*, 544 U.S. 93, 102 (2005); *Roberts* v. *Galen of Va., Inc.*, 525 U.S. 249, 253-254 (1999). That practice is particularly appropriate here, where *no* court has previously addressed whether these particular types of rates are contract rates. This Court is "a court of review, not of first view." *Cutter* v. *Wilkinson*, 544 U.S. 709, 718 n.7 (2005). Accordingly, the Court should leave respondents' alternative argument to be addressed, if at all, by the court of appeals in the first instance on remand.

B. The Rates at Issue Are "Contract Rates" Entitled to *Mobile-Sierra* Protection

Respondents' alternative ground is, in any event, without merit. *Mobile-Sierra* distinguishes between "contract rates" agreed upon bilaterally (or multilaterally) by

the parties and rates set "unilaterally by tariff." See *Morgan Stanley*, 128 S. Ct. at 2738-2740, 2746 n.3, 2749 n.6. Contract rates are entitled to *Mobile-Sierra* protection; unilateral tariff rates normally are not. See *ibid.*; pp. 21-22, *supra*.

The auction rates and transition payments are both contract rates. The results of the capacity auctions are clearly contracts—voluntary agreements for the sale of capacity between sellers and buyers who choose to participate in the auctions—wholly apart from the settlement. Those auction results would be contracts protected by *Mobile-Sierra* even absent a settlement agreement of any sort. FERC could not have exceeded its authority by approving a settlement provision that merely recited the standard that would apply in any event. The settling parties' transition-payment obligations are likewise contract rates, not unilateral tariff rates. Those fixed rates are expressly set forth in a contract—the settlement agreement—to which the settling parties agreed.

1. *The Auction Rates Are Contract Rates*

a. Respondents' contention that auction rates are not contract rates entitled to *Mobile-Sierra* protection ignores the black-letter rule that a sale by auction *is* a contract. The participant's bid constitutes the contractual "offer," and the auctioneer "accepts" the offer "by the fall of the hammer or in other customary manner." U.C.C. §2-328(2); see *Restatement (Second) of Contracts* §28(1)(a) (1981); 1 *Williston on Contracts* §4:12, at 515-527; 1 J. Perillo, *Corbin on Contracts* §4.14, at 637-645 (rev. ed. 1993).[11] Auctions thus result in the same binding

[11] By contrast, in an auction "without reserve"—where the auctioneer waives his right to withdraw the goods—the auctioneer's announcement constitutes the "offer" and the bid constitutes the "acceptance." See *Restatement (Second) of Contracts* §28(1)(b). Capa-

obligations as any other sales contract: "The bidder in an auction * * * is obligated generally to fulfill his or her promise by paying the price bid. * * * [H]e or she is entitled to have the property delivered to him or her, and a refusal of delivery is a *breach of contract*." 7 Am. Jur. 2d *Auctions and Auctioneers* §§49, 52, at 398, 402 (1997) (emphasis added); see also 7A C.J.S. *Auctions and Auctioneers* §53, at 642 (2004) (where winning bidder fails to pay, "the seller is justified in treating the contract as breached or rescinded"); cf. 1 *Corbin on Contracts* §4.14, at 642 ("It is obvious that after a bid has been made, at a sale 'without reserve,' there is a contract * * * .").[12]

The capacity auctions are no exception. They produce voluntary contracts, not unilateral tariffs. In each auction, suppliers compete to provide capacity for a period of one year (or up to five years in the case of new entrants) starting three years after the auction. See Pet. App. 110a-111a; J.A. 98-99, 105. Before each auction, ISO-NE determines the amount of capacity it will purchase—the "installed capacity requirement"—according to processes it develops in consultation with utilities and other stakeholders. See Pet. App. 118a; J.A. 59-60, 70, 121-123; *ISO New England, Inc.*, 118 F.E.R.C. ¶61,157, at 61,758 (2007). The auction then follows a descending price format. See J.A. 131. The auctioneer announces a starting price, and suppliers decide how much capacity to offer at that price. J.A. 66. If the bidders offer more capacity at that price than is needed, the price drops, and each supplier again decides how much to offer. *Ibid.* That proc-

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city auctions arguably fall into that category, but nothing turns on the distinction.

[12] The capacity auctions are "reverse auctions" in which sellers alter their offers in response to the auctioneer's prices, but the results are contracts regardless.

ess repeats itself until supply equals demand. *Ibid.* The resulting price is the "clearing price," and the remaining bidders are the winners. *Ibid.* They are committed to provide the capacity they offered for the prescribed period, and are entitled to receive the clearing price in return. See Pet. App. 110a-111a; J.A. 66, 149.

No utility is required to purchase capacity at the auction clearing price. Under the settlement agreement's "self-supply" provisions, utilities can "meet [their] capacity obligations without paying the auction clearing price" by contracting for capacity outside the auction or supplying it themselves. Pet. App. 112a; see J.A. 65, 84-85, 111-112, 142, 149.[13] Those that choose to acquire capacity through the auction, however, are responsible for paying for capacity at the auction price in proportion to their share of peak usage. See Pet. App. 112a; J.A. 70. Like any other contract rate, therefore, the auction rates reflect voluntary agreements between buyers and sellers.

By contrast, auction rates bear no resemblance to the unilateral tariffs subject to ordinary just-and-reasonable review. No single supplier dictates when the auction will end or what the clearing price will be. To the contrary, the outcome is determined by an iterative, multilateral

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[13] Purchasers planning to self-supply must designate and qualify their generating resources in advance of the auction. See J.A. 111-112. Those resources are still "offered into" the auction in the sense that they offset a portion of the installed capacity requirement, see *id.* at 65, 112, but payments are set by the contract rather than the auction clearing price, see *id.* at 149; Pet. App. 112a. Market participants have in fact invoked the self-supply provision to acquire capacity by contract. See ISO New England Inc., *Internal Market Monitoring Unit Review of the Forward Capacity Market Auction Results and Design Elements* 32-33 (June 5, 2009), available at http://www.iso-ne.com/regulatory/ferc/filings/index.html (noting "994 MW of resources * * * under state contracts in Connecticut").

process in which many sellers and buyers participate. Auctions are a more sophisticated and competitive contracting process, but they still result in contracts by which buyers agree to purchase capacity from sellers at a specified rate. Cf. *Richmond Power & Light* v. *FPC*, 481 F.2d 490, 496-497 (D.C. Cir. 1973) (*Mobile-Sierra* "appl[ies] whether the parties agree to a specific rate or whether they agree to a rate changeable in a specific manner").

Respondents repeatedly urge that they should be allowed to challenge auction rates under the ordinary just-and-reasonable standard because they did not agree to the *settlement agreement*. See, *e.g.*, Br. in Opp. 15-17. But the fact that the settlement was contested does not alter the fact that auction results are voluntary contracts among willing auction participants. Where a utility has chosen to acquire capacity through the auction, rather than contracting for it elsewhere under the self-supply provisions, its commitment is a voluntary contract. The fact that a complainant objected to one contract (the settlement agreement) does not mean it is entitled to a different standard of review for another contract (the auction result). If the auctions were held in the absence of any settlement agreement, the resulting rates would unquestionably be contract rates entitled to *Mobile-Sierra* protection. FERC cannot have erred in approving a settlement provision that merely recited the standard that would apply to auction results even absent a settlement.

b. The rationales underlying *Mobile-Sierra* also apply with full—if not special—force here. First, just as "'sophisticated businesses enjoying presumptively equal bargaining power * * * could be expected to negotiate a "just and reasonable" rate,'" *Morgan Stanley*, 128 S. Ct. at 2746, sophisticated businesses participating in capacity

auctions can be expected to arrive at a just-and-reasonable rate. As Judge Tatel observed when addressing these very auctions: "[T]he point of an auction mechanism like the Forward Market is to use a best approximation of demand and the power of competitive bidding to help locate [an efficient] price. * * * [T]he real world decision makers who use the Forward Market do so precisely for its ability to evaluate prices." *Conn. Dep't of Pub. Util. Control* v. *FERC*, Nos. 07-1375 *et al.*, 2009 WL 1754607, at *7 (D.C. Cir. June 23, 2009); see also J.A. 67-68; Pet. App. 138a. Economists likewise widely laud auctions—particularly single-clearing-price auctions—as a means "to reliably provide consumers electricity at minimum cost." Cramton & Stoft, *Why We Need to Stick with Uniform-Price Auctions in Electricity Markets*, Electricity J., Jan./Feb. 2007, at 26, 26-27.[14] These particular auctions, moreover, include various refinements to ensure that prices are set competitively. See Pet. App. 115a-116a. In addition, FERC approved the auction structure under the ordinary just-and-reasonable standard, *id.* at 135a-144a, and can review auction results under that standard for 45 days following each auction, see *id.* at 78a, 120a, 202a. Although not necessary for *Mobile-Sierra* to apply, see *Morgan Stanley*, 128 S. Ct. at 2745-2746, FERC's approval and ongoing oversight corroborate the expectation of reasonableness.

The need for contract stability is likewise compelling here. As FERC explained, "[s]tability is particularly im-

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[14] See also Baldick, *Single Clearing Price in Electricity Markets* (2009), http://www.competecoalition.com/files/Baldick%20study.pdf; Kahn, *et al.*, *Uniform Pricing or Pay-as-Bid Pricing*, Electricity J., July 2001, at 70, 71-72. Professor Cramton also testified favorably regarding the proposed auction mechanism on behalf of ISO-NE below. See J.A. 41; C.A. App. 1790-1808.

portant in this case, which was initiated in part because of the unstable nature" of New England's capacity market and the resulting chronic shortage of generating capacity. See Pet. App. 202a; p. 9, *supra*. The auctions take place a full three years before capacity is needed so suppliers can plan and build new facilities. See Pet. App. 110a; J.A. 68-69. But auctions cannot create adequate incentives to build hundreds of millions of dollars' worth of infrastructure if the resulting prices are subject to revision years into the contract. See pp. 37-41, *supra*. As FERC observed, "[t]he Court's statement in *Mobile* that 'all agree . . . [that] the stability of supply arrangements . . . is essential to the health of the natural gas industry' is no less true with regard to the health of New England's electricity infrastructure." Pet. App. 203a (quoting 350 U.S. at 344). The need for stability is thus at least as pressing here as it was in *Mobile*, *Sierra*, or *Morgan Stanley*. And, because the auction rates are contract rates rather than unilateral tariffs, they are entitled to the stability that *Mobile-Sierra* provides.

2. *The Transition Payments Are Contract Rates*

Respondents' contention that the transition payments are not contract rates protected by *Mobile-Sierra* likewise fails. As an initial matter (and as explained at the petition stage, Pet. Reply 7 n.2), there is little and rapidly diminishing reason to address the issue. Unlike the annual auctions, the transition payments terminate at the end of May 2010. J.A. 163-164. Following extensive proceedings, FERC reviewed those rates under the ordinary just-and-reasonable standard and rejected respondents' challenges to them. See Pet. App. 140a-161a. Respondents have identified no changed circumstance that might justify a different result now—under *any* standard—and the likelihood of one emerging between now

and May 2010 is remote. This issue should be addressed, if at all, by the court of appeals in the first instance on remand.

In any event, the transition-payment obligations *of the settling parties* are clearly "contract rates" entitled to *Mobile-Sierra* protection. The settlement agreement sets forth a fixed schedule of rates that settling buyers agree to pay sellers for capacity for specified periods—a classic *Mobile-Sierra* contract. See J.A. 163-164. That the terms are set forth in a settlement that resolves pending litigation does not make the agreement any less a "contract" (whatever else it might also be). See *Kokkonen* v. *Guardian Life Ins. Co. of Am.*, 511 U.S. 375, 381 (1994); *Firefighters*, 478 U.S. at 515-524; cf. *Cities of Bethany* v. *FERC*, 727 F.2d 1131, 1139 (D.C. Cir. 1984). Like any other contract rate, those rates were negotiated by sophisticated market participants and thus can be expected to be reasonable. And FERC specifically noted the need to "increase the stability of the market during the transition period." Pet. App. 159a-160a. FERC thus did not err in concluding that the settling parties' transition-payment obligations could not be overturned—whether challenged by the settling parties themselves or by others indirectly affected by the settling parties' obligations—absent the showing that *Mobile-Sierra* requires.[15]

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[15] Respondents argue that the transition payments more closely resemble a unilateral tariff to the extent any *non-settling* party (such as NSTAR) must itself make those payments. See Br. in Opp. 11; cf. *ITC Holdings Corp.*, 102 F.E.R.C. ¶61,182, at 61,491 (2003) (rationale for *Mobile-Sierra* "does not apply * * * [to] a contract that is essentially seeking to set not only the respective rights and obligations of the contractual parties, but also the rates that third parties will pay"). Whether transition-payment obligations imposed on non-signatories would be contract or unilateral tariff rates, and whether

CONCLUSION

For the foregoing reasons, the court of appeals' decision should be reversed.

FERC could impose *Mobile-Sierra* protection even in the latter event, are complex questions that this Court should not address in the first instance. See pp. 45-46, *supra*. The record makes clear, however, that NSTAR had a full and fair opportunity to challenge the level of transition payments under the ordinary just-and-reasonable standard, see Pet. App. 120a-121a & n.32, 144a-147a; that NSTAR lost on that issue before FERC, *id.* at 151a-161a; and that NSTAR lost on that issue again before the court of appeals, *id.* at 8a-15a. NSTAR cannot, consistent with ordinary *res judicata* principles, expect to resurrect its challenge absent a significant change of circumstances. In any event, the settlement does not in fact directly impose transition-payment obligations on non-parties. The transition payments are actually made by *ISO-NE*, which bills load-serving entities for their shares. See ISO New England, Inc., *Manual for Billing (M-29)* §§ 1.1.1(1)(i), 1.1.6 & revision 13 (16th rev. Sept. 5, 2008), available at http://www.iso-ne.com/rules_proceds/isone_mnls/index.html. Because ISO-NE signed the settlement agreement, see J.A. 90, the payment obligations are classic contract rates entitled to *Mobile-Sierra* protection; the fact that those obligations indirectly affect load-serving entities like NSTAR provides no basis for treating them differently from any other contract rate. Moreover, the widespread support for the transition payments provides a strong basis for expecting them to be reasonable. See *id.* at 89-91. If the agreement of *two* parties (a single buyer-seller pair) creates a presumption of reasonableness, the agreement of *dozens* of buyers and sellers creates a stronger presumption still. The need for contract stability, moreover, is still acute. See Pet. App. 158a-160a. Thus, even if *Mobile-Sierra* would not *compel* FERC to apply the public-interest standard in these circumstances, FERC's considered decision to apply that standard is entitled to respect.

Respectfully submitted.

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JULY 2009

RESPONDENT'S BRIEF

No. 08-674

In the Supreme Court of the United States

NRG POWER MARKETING, LLC, ET AL., PETITIONERS

v.

MAINE PUBLIC UTILITIES COMMISSION, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION

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QUESTION PRESENTED

Whether the principles set out in this Court's decisions in *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956), and *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956), apply to the Federal Energy Regulatory Commission's review of wholesale electricity rates set by contract when those rates are challenged by a non-contracting party.

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BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-27a) is reported at 520 F.3d 464. The orders of the Federal Energy Regulatory Commission (Pet. App. 28a-101a, 102a-223a) are reported at 115 F.E.R.C. ¶ 61,340 and 117 F.E.R.C. ¶ 61,133.

JURISDICTION

The judgment of the court of appeals was entered on March 28, 2008. A petition for rehearing was denied on October 6, 2008 (Pet. App. 241a-248a). The petition for a writ of certiorari was filed on November 21, 2008. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. a. The Federal Power Act (FPA or Act), 16 U.S.C. 791a *et seq.*, grants the Federal Energy Regulatory Commission (Commission or FERC) exclusive jurisdiction over the "transmission of electric energy in interstate commerce" and the "sale of electric energy at wholesale in interstate commerce" by public utilities. 16 U.S.C. 824(b)(1). Proposed rates for the sale or transmission of power within FERC's jurisdiction are subject to FERC review to ensure that they are "just and reasonable" and not unduly discriminatory or preferential. 16 U.S.C. 824d(a) and (b). To that end, the FPA provides:

> Under such rules and regulations as the Commission may prescribe, every public utility shall file with the Commission, within such time and in such form as the Commission may designate, * * * schedules showing all rates and charges for any transmission or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

16 U.S.C. 824d(c).

b. In *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956) (*Mobile*), this Court interpreted provisions of the Natural Gas Act (NGA), 15 U.S.C. 717 *et seq.*, that parallel the FPA. The Court held that, "by requiring contracts to be filed with the Commission, the Act expressly recognizes that rates to particular customers may be set by individual contracts." *Mobile*, 350 U.S. at 338. The Court further concluded that the NGA does not empower a natural gas

company unilaterally to modify its contracts with its customers. *Id.* at 343. "By preserving the integrity of contracts," the Court observed, the statute promotes "the stability of supply arrangements which all agree is essential to the health of the natural gas industry." *Id.* at 344. "On the other hand, denying to natural gas companies the power unilaterally to change their contracts in no way impairs the regulatory powers of the Commission, for the contracts remain fully subject to the paramount power of the Commission to modify them when necessary in the public interest." *Ibid.*

On the same day that it issued its decision in *Mobile*, the Court held in *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956) (*Sierra*), that the FPA, like the NGA, did not authorize unilateral contract changes by the contracting parties. *Id.* at 353. The Court in *Sierra* also addressed the scope of the Commission's authority under 16 U.S.C. 824e(a) to change rates if it finds them to be "unjust, unreasonable, unduly discriminatory or preferential." In the underlying orders, the Commission had found a rate set by a contract to be unreasonable because it failed to yield the seller a reasonable rate of return. *Sierra*, 350 U.S. at 354. The Court held that the Commission had applied the wrong standard in reviewing the contract: "[W]hile it may be that the Commission may not normally *impose* upon a public utility a rate which would produce less than a fair return," a utility nevertheless may agree by contract to accept such a rate, and, if it does so, it is not "entitled to be relieved of its improvident bargain." *Id.* at 355.

Instead, the Court explained, "the sole concern of the Commission would seem to be whether the rate is so low as to adversely affect the public interest—as where it might impair the financial ability of the public utility to

continue its service, cast upon other customers an excessive burden, or be unduly discriminatory." *Sierra*, 350 U.S. at 355. The Court found this focus on the "public interest," as distinguished from the private interests of the utilities, to be evidenced by the recital in 16 U.S.C. 824(a) that the scheme of regulation imposed by the Act "is necessary in the public interest." *Sierra*, 350 U.S. at 355 (quoting 16 U.S.C. 824(a)). The Court therefore instructed that the matter be remanded to the Commission for further proceedings, noting that "[w]hether under the facts of this case the contract rate is so low as to have an adverse effect on the public interest is of course a question to be determined in the first instance by the Commission." *Ibid.*

2. This case involves the "capacity" market for electricity in New England. In a capacity market, unlike a wholesale energy market, an electricity provider purchases from a generator the option to buy a specific quantity of energy, regardless of whether the energy itself is ultimately purchased. Pet. App. 2a. Providers make such purchases in order to maintain the reliability of the electric grid—by purchasing more capacity than their customers' expected demand, providers can ensure that they are able to respond adequately to unexpected demand fluctuations. *Ibid.*

For many years, there were significant problems in the New England capacity market: generators were earning insufficient revenue, and therefore insufficient infrastructure was being developed, resulting in a barely sufficient supply of capacity. Pet. App. 2a. FERC, the generators, the electricity providers, and the power customers made several unsuccessful attempts to address those issues. *Ibid.* Ultimately, a settlement was

reached, with only eight of 115 parties opposing the settlement. *Id.* at 5a.

The key feature of the settlement was the creation of a Forward Capacity Market, under which there would be annual auctions for capacity, held three years in advance of when the capacity was needed. Pet. App. 5a. In the three-year gap between the first auction and the time when capacity purchased in that auction would be provided, the settlement provided for a series of fixed transition payments to be paid to generators. *Id.* at 6a. Under Section 4.C of the settlement agreement, future challenges to the transition payments or to the final prices from the auctions would be reviewed under the *Mobile-Sierra* "public interest" standard, "whether the change is proposed by a Settling Party, a non-Settling Party, or the FERC acting *sua sponte*." *Id.* at 193a-194a.

The Commission approved the settlement, finding that, "as a package, it presents a just and reasonable outcome for this proceeding consistent with the public interest." Pet. App. 103a. Most significantly, the settlement would resolve the problems in the New England capacity market by establishing "the appropriate market structure to ensure that generating resources are appropriately compensated based on their location and contribution to system reliability" and by "provid[ing] incentives to attract new infrastructure where needed." *Id.* at 142a. The Commission also determined that the *Mobile-Sierra* provision in Section 4.C "appropriately balances the need for rate stability and the interests of the diverse entities who will be subject to" the Forward Capacity Market. *Id.* at 202a. The Commission explained that "[s]tability is particularly important in this case, which was initiated in part because of the unstable

nature of [installed capacity] revenues and the effect that has on generating units, particularly those who are critical to maintaining reliability." *Ibid.* It concluded that the *Mobile-Sierra* provision would not operate to the detriment of parties not agreeing to the settlement, because the Commission would retain significant authority under *Mobile-Sierra* to protect non-parties to the contract. *Id.* at 201a; *id.* at 69a-70a.

3. The court of appeals rejected various challenges to the Commission's approval of the settlement agreement, but it granted petitions for review to the extent that they challenged the approval of the *Mobile-Sierra* clause. Pet. App. 1a-27a.

The court of appeals held that, under *Mobile-Sierra*, "when the parties to a rate dispute reach a contractual settlement, FERC must enforce the terms of the bargain unless the public interest requires otherwise." Pet. App. 20a. But the court held that the Commission may not approve a settlement agreement applying the *Mobile-Sierra* standard to rate challenges brought by non-contracting (or non-settling) third parties. *Ibid.* In the court's view, the *Mobile-Sierra* doctrine carves out an "exception" to the generally applicable just-and-reasonable standard for claims brought by the contracting parties, and it is intended to "make it more difficult for either party to shirk its contractual obligations." *Id.* at 20a, 24a. The court held that the application of *Mobile-Sierra* to non-settling parties would "deprive[] non-settling parties of their statutory right to have rate challenges adjudicated under the 'just and reasonable' standard." *Id.* at 22a. Instead, the court concluded, "[w]hen a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply;

the proper standard of review remains the 'just and reasonable' standard." *Ibid.*

4. After the court of appeals issued its decision, this Court decided *Morgan Stanley Capital Group, Inc.* v. *Public Utility District No. 1*, 128 S. Ct. 2733 (2008) (*Morgan Stanley*). In that case, the Court held that "[t]here is only one statutory standard for assessing wholesale electricity rates, whether set by contract or tariff—the just-and-reasonable standard." *Id.* at 2745. Instead of representing a standard different from the just-and-reasonable standard, the *Mobile-Sierra* "'public interest standard' refers to the differing *application* of the just-and-reasonable standard to contract rates." *Id.* at 2740. The Court explained that *Mobile-Sierra*'s "definition of what it means for a rate to satisfy the just-and-reasonable standard" is "a definition that applies regardless of when the contract is reviewed," and therefore the application of *Mobile-Sierra* does not depend on when a contract rate is challenged. *Id.* at 2746. And the Court held that *Mobile-Sierra* applies equally to challenges by buyers and sellers; in either case, "[t]he contract rate must seriously harm the public interest" before it may be set aside. *Id.* at 2747.

5. After *Morgan Stanley* was decided, several parties to this case, including FERC, petitioned for rehearing en banc. The court of appeals denied the petitions. Pet. App. 245a-248a.

6. The court of appeals issued its mandate, and on remand, the Commission "approve[d] the settlement conditioned on the settling parties revising the standard of review applicable to non-settling third parties, consistent with the court's decision." 126 F.E.R.C. ¶ 61,027 at para. 5 (2009).

ARGUMENT

Petitioners contend (Pet. 14-15) that the decision of the court of appeals "destroys the certainty and stability that the electricity and natural gas markets require and that *Mobile-Sierra* attempts to provide." The decision below does not conflict with any decision of any other court of appeals, and petitioners overstate its practical significance. Plenary review by this Court is not warranted. The decision of the court of appeals preceded this Court's decision in *Morgan Stanley Capital Group, Inc.* v. *Public Utility District No. 1*, 128 S. Ct. 2733 (2008), however, and that decision may inform the proper resolution of this case. Accordingly, the petition for a writ of certiorari should be granted, the judgment of the court of appeals vacated in relevant part, and the case remanded for further consideration in light of *Morgan Stanley*.

1. Petitioners assert (Pet. 25) that the decision of the court of appeals conflicts with "decades of settled practice" in the application of *Mobile-Sierra*, but none of the cases they cite considered the issue presented here, namely, whether contracting parties can impose the *Mobile-Sierra* presumption on future rate complaints brought by non-contracting parties. With the exception of *Town of Norwood* v. *FERC*, 587 F.2d 1306, 1309 (D.C. Cir. 1978), which involved a declaratory action brought by one of the contracting parties, each of the cases involved a Commission-initiated investigation under 16 U.S.C. 824e. While non-parties to the contracts at issue raised arguments in the proceedings, the rate investigations were initiated by the Commission in response to utility rate filings made under 16 U.S.C. 824d, and they were not the result of third-party complaints, as in this case. Thus, the cases stand for nothing more

than the proposition that the *Mobile-Sierra* public interest approach applies when a contract is challenged by a party to the contract or by the Commission acting on its own initiative under Section 824e.

The decision below does not conflict with that proposition. In fact, the court of appeals has previously held that parties may bind themselves and the Commission to review under the *Mobile-Sierra* presumption. See *Papago Tribal Util. Auth.* v. *FERC*, 723 F.2d 950, 953 (D.C. Cir. 1983) (Scalia, J.) ("[B]y broad waiver, the parties may eliminate both the utility's right to make immediately effective rate changes under [Section 824d] and the Commission's power to impose changes under [Section 824e], except the indefeasible right of the Commission under [Section 824e] to replace rates that are contrary to the public interest."), cert. denied, 467 U.S. 1241 (1984); see also *Maine Pub. Utils. Comm'n* v. *FERC*, 454 F.3d 278, 283 (D.C. Cir. 2006). But that proposition does not resolve the analytically distinct question presented here: whether the *Mobile-Sierra* application of the just-and-reasonable standard governs rate challenges initiated by non-contracting parties.

2. While the Commission argued in its petition for rehearing en banc that the decision of the court of appeals raises significant policy concerns, those concerns do not rise to the level suggested by petitioners here (Pet. 19-23). There is no doubt that *Mobile-Sierra* protections promote contract stability: that fact informed the Commission's unanimous decision to approve the *Mobile-Sierra* clause in the settlement at issue here. Pet. App. 202a ("Stability is particularly important in this case, which was initiated in part because of the unstable nature of [installed capacity] revenues and the effect that has on generating units, particularly those

who are critical to maintaining reliability."). But petitioners overstate the extent to which the decision below undermines that stability, and, in the absence of a direct circuit conflict, the practical consequences of the decision have not been shown to be so significant as to warrant plenary review by this Court at this time.

Petitioners suggest (Pet. 19, 21) that the decision below could lead to widespread contract modification at the behest of a "boundless group" of interested parties. But the ordinary just-and-reasonable standard would itself furnish substantial protection for established rates such as those at issue here, and it gives the Commission discretion to take into account the facts and circumstances of the particular rate, term, or condition that is being challenged. See, *e.g.*, *Montana-Dakota Utils. Co.* v. *Northwestern Pub. Serv. Co.*, 341 U.S. 246, 251 (1951) ("Statutory reasonableness is an abstract quality represented by an area rather than a pinpoint. It allows a substantial spread between what is unreasonable because too low and what is unreasonable because too high."); *Permian Basin Area Rate Cases*, 390 U.S. 747, 767 (1968) ("[T]his Court has often acknowledged that the Commission is not required by the Constitution or the Natural Gas Act to adopt as just and reasonable any particular rate level; rather, courts are without authority to set aside any rate selected by the Commission which is within a 'zone of reasonableness.'") (quoting *FPC* v. *Natural Gas Pipeline Co.*, 315 U.S. 575, 585 (1942)); cf. *Global Crossing Telecomms., Inc.* v. *Metrophones Telecomms, Inc.*, 550 U.S. 45, 57-58 (2007). Accordingly, even in the absence of the *Mobile-Sierra* clause in the settlement, the Commission may take into account, in addressing future challenges by non-settling third parties to either the transition payments or For-

ward Contract Market auction results, the importance of the settlement rates in assuring basic resource adequacy and maintaining reliability.

Petitioners also express concern (Pet. 19) that, under the ordinary just-and-reasonable standard, contracts may be abrogated based on changing market conditions that make them "temporarily[] unattractive" to third parties. But "[t]he FPA recognizes that contract stability ultimately benefits consumers, even if short-term rates for a subset of the public might be high by historical standards—which is why it permits rates to be set by contract and not just by tariff." *Morgan Stanley*, 128 S. Ct. at 2749. A settlement may be just and reasonable when reviewed in its totality, even if, in the short run, the rate seems high. The Commission generally examines the reasonableness of a contract rate over the life of the contract, and not just in a single year. *Northern Va. Elec. Coop., Inc.*, 116 F.E.R.C. ¶ 61,173 at 61,741 (2006) (*NOVEC*). Commission precedent also typically requires rate challengers to show changed circumstances in order to obtain a rate change, even under the ordinary application of the just-and-reasonable standard. See, *e.g.*, *Dynegy Moss Landing, LLC*, 123 F.E.R.C. ¶ 61,280 at 62,724 (2008); *NOVEC*, 116 F.E.R.C. ¶ 61,173 at 61,741.

Finally, petitioners argue (Pet. 22) that the decision of the court of appeals will permit contracting parties to evade the *Mobile-Sierra* presumption by recruiting a non-party to join them in challenging rates. While the decision does have the anomalous result of imposing a higher standard on contracting parties and the Commission acting on its own initiative than on non-parties challenging contract rates, the Commission should be able to mitigate that anomalous result by rejecting rate chal-

lenges that amount to inappropriate strategic behavior, such as a third-party complaint challenging a contract filed by a proxy for one of the contracting parties.*

3. Although this case does not warrant plenary review at this time, the Court should grant the petition for a writ of certiorari, vacate the decision below insofar as it rejected the Commission's ruling on the *Mobile-Sierra* issue and therefore granted the petitions for review to that extent, and remand for further consideration in light of *Morgan Stanley*. The court of appeals panel did not have the benefit of *Morgan Stanley* when it considered how to apply *Mobile-Sierra* principles in the context of the settlement agreement at issue here. In its petition for rehearing, the Commission argued that the decision below "directly conflicts with the subsequently-issued Supreme Court decision in *Morgan Stanley*." FERC Reh'g Pet. 2; but see Pet. App. 224a-240a (dissenting opinion of two members of the Commission). It is not necessary, however, for this Court to determine whether there is a conflict with *Morgan Stanley*. Whether or not a conflict exists, *Morgan Stanley* is undoubtedly relevant to this case, and it represents an "'intervening development[]'" that, at a minimum, creates "a 'reasonable probability' that the Court of Appeals [will] reject a legal premise on which it relied and which may affect the outcome of the litigation." *Tyler* v. *Cain*, 533 U.S. 656, 666 n.6 (2001) (quoting *Lawrence* v. *Chater*, 516 U.S. 163, 167 (1996)).

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* Petitioners express concern (Pet. 21-22) that the Ninth Circuit, on remand from this Court in *Morgan Stanley*, might apply the reasoning of the decision below. The Ninth Circuit has not done so but has instead remanded the case to the Commission to allow it to consider the issues remanded by this Court. *Public Utils. Comm'n* v. *FERC*, 550 F.3d 767 (2008).

There are at least two ways in which *Morgan Stanley* may inform the analysis of the court of appeals. First, the court of appeals stated that "[t]he *Mobile-Sierra* doctrine carves out an exception" to the statutory "just and reasonable" standard. Pet. App. 20a. It is possible that the court simply meant that *Mobile-Sierra* principles subject contract rates to a different *application* of the just-and-reasonable standard—in that sense, it would be correct to say *Mobile-Sierra* provides for an "exception" to the ordinary application of "just and reasonable" review. Cf. *Morgan Stanley*, 128 S. Ct. at 2740. But the court of appeals' language leaves open the possibility that the court failed to appreciate that "[t]here is only one statutory standard for assessing wholesale electricity rates, whether set by contract or tariff—the just-and-reasonable standard." *Id.* at 2745; see Pet. App. 22a (suggesting that application of *Mobile-Sierra* would "deprive[] non-settling parties of their statutory right to have rate challenges adjudicated under the 'just and reasonable' standard"). *Morgan Stanley* made clear that *Mobile-Sierra* is not an exception to the application of the just and reasonable standard; it simply "provide[s] a definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context." 128 S. Ct. at 2746.

Second, the court of appeals stated that "the *Mobile-Sierra* doctrine is designed to ensure contract stability *as between the contracting parties—i.e.*, to make it more difficult for either party to shirk its contractual obligations." Pet. App. 24a. That line of reasoning is similar to the Ninth Circuit's interpretation of *Mobile-Sierra* "as the equivalent of an estoppel doctrine," an interpretation that this Court rejected in *Morgan Stanley*. 128 S. Ct. at 2746. *Morgan Stanley* held that *Mobile-Sierra*

rests not on principles of estoppel but rather on a "presum[ption] that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law." *Id.* at 2737. That presumption would not necessarily cease to apply simply because the challenge to the rate came from a non-contracting party.

The court of appeals should be given an opportunity to reconsider its analysis in light of *Morgan Stanley* and to determine how, if at all, the judgment should be altered, taking into account that decision and the action that the Commission has already taken to implement the judgment. A grant, vacatur, and remand is therefore appropriate.

CONCLUSION

The petition for a writ of certiorari should be granted, the judgment of the court of appeals vacated insofar as it granted the petitions for review, and the case remanded for further consideration in light of *Morgan Stanley Capital Group Inc.* v. *Public Utility District No. 1*, 128 S. Ct. 2733 (2008).

Respectfully submitted.

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RESPONDENT'S BRIEF

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In the Supreme Court of the United States

NRG POWER MARKETING, LLC, ET AL., PETITIONERS

v.

MAINE PUBLIC UTILITIES COMMISSION, ET AL.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION

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QUESTION PRESENTED

Whether the Federal Energy Regulatory Commission had authority to approve a settlement containing a provision specifying that the review of certain aspects of the rates, terms, and conditions for the sale of electric capacity should be governed by the principles set out in this Court's decisions in *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956), and *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956).

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BRIEF FOR THE
FEDERAL ENERGY REGULATORY COMMISSION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-27a) is reported at 520 F.3d 464. The orders of the Federal Energy Regulatory Commission (Pet. App. 28a-101a, 102a-223a) are reported at 115 F.E.R.C. ¶ 61,340 and 117 F.E.R.C. ¶ 61,133.

JURISDICTION

The judgment of the court of appeals was entered on March 28, 2008. Petitions for rehearing were denied on October 6, 2008 (Pet. App. 241a-242a, 243a-244a, 245a-246a, 247a-248a). The petition for a writ of certiorari was filed on November 21, 2008, and was granted on April 27, 2009. The jurisdiction of this Court rests on 28 U.S.C. 1254(1).

STATUTORY PROVISIONS INVOLVED

Pertinent statutory provisions are set forth in an appendix to this brief. App., *infra*, 1a-14a.

STATEMENT

1. a. The Federal Power Act (FPA or Act), 16 U.S.C. 791a *et seq.*, grants the Federal Energy Regulatory Commission (FERC or Commission) exclusive jurisdiction over the "transmission of electric energy in interstate commerce" and the "sale of electric energy at wholesale in interstate commerce" by public utilities. 16 U.S.C. 824(b)(1). Under the FPA, proposed rates for the sale or transmission of power within FERC's jurisdiction must be "just and reasonable" and not unduly discriminatory or preferential. 16 U.S.C. 824d(a) and (b). To facilitate the Commission's exercise of its regulatory responsibilities, the FPA provides for rates and related matters to be filed with the Commission:

> Under such rules and regulations as the Commission may prescribe, every public utility shall file with the Commission, within such time and in such form as the Commission may designate, * * * schedules showing all rates and charges for any transmission or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

16 U.S.C. 824d(c).

The Act also provides for the Commission to review rates after they have been accepted for filing and gone into effect. If, after a hearing—either on its own motion or based on a complaint—the Commission determines

that any existing rate or charge is "unjust, unreasonable, unduly discriminatory or preferential," it must determine and fix by order "the just and reasonable rate * * * to be thereafter observed and in force." 16 U.S.C. 824e(a).

b. The parties to a proceeding before the Commission, including a proceeding under Section 824e, may agree to a settlement. If a proposed settlement is "uncontested"—that is, if it is agreed to by all of the parties to the proceeding—the Commission may approve it "upon a finding that the settlement appears to be fair and reasonable and in the public interest." 18 C.F.R. 385.602(g)(3). If a proposed settlement is contested by one or more parties, "the Commission may decide the merits of the contested settlement issues, if the record contains substantial evidence upon which to base a reasoned decision or the Commission determines there is no genuine issue of material fact." 18 C.F.R. 385.602(h)(1)(i). The Commission may review and approve a contested settlement "as a package" so long as it determines that "the overall result * * * is just and reasonable." *Trailblazer Pipeline Co.*, 85 F.E.R.C. ¶ 61,345, at 62,342 (1998), order on denial of reh'g, 87 F.E.R.C. ¶ 61,110 (1999) (*Trailblazer*). Such a determination does not require a finding "that the settlement rate is exactly the rate the Commission would establish on the merits after litigation," but only that it is "within a broad ambit of various rates which may be just and reasonable." *Id.* at 62,343.

c. In *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956) (*Mobile*), this Court interpreted provisions of the Natural Gas Act (NGA), 15 U.S.C. 717 *et seq.*, that parallel the FPA. The Court held that, "by requiring contracts to be filed with the

Commission, the Act expressly recognizes that rates to particular customers may be set by individual contracts." *Mobile*, 350 U.S. at 338. The Court further concluded that the NGA does not empower a natural-gas company unilaterally to modify its contracts with customers by filing a new rate schedule with the Commission. *Id.* at 343. "By preserving the integrity of contracts," the Court observed, the statute promotes "the stability of supply arrangements which all agree is essential to the health of the natural gas industry." *Id.* at 344. "On the other hand, denying to natural gas companies the power unilaterally to change their contracts in no way impairs the regulatory powers of the Commission, for the contracts remain fully subject to the paramount power of the Commission to modify them when necessary in the public interest." *Ibid.*

On the same day that it issued its decision in *Mobile*, the Court held in *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956) (*Sierra*), that the FPA, like the NGA, does not authorize unilateral contract changes by a contracting party through the filing of a new rate schedule. *Id.* at 353. The Court in *Sierra* also addressed the scope of the Commission's authority under 16 U.S.C. 824e(a) to determine and fix a new rate if it finds the existing rate to be "unjust, unreasonable, unduly discriminatory or preferential." In the underlying orders, the Commission had found a rate set by contract to be unreasonable because it failed to yield the seller a reasonable rate of return. 350 U.S. at 354. The Court held that the Commission had applied the wrong standard in reviewing the contract: "[W]hile it may be that the Commission may not normally *impose* upon a public utility a rate which would produce less than a fair return," a utility nevertheless may agree by contract to accept such a rate, and

if it does so, it is not "entitled to be relieved of its improvident bargain." *Id.* at 355.

Instead, the *Sierra* Court explained, "the sole concern of the Commission would seem to be whether the rate is so low as to adversely affect the public interest—as where it might impair the financial ability of the public utility to continue its service, cast upon other customers an excessive burden, or be unduly discriminatory." 350 U.S. at 355. The Court found this focus on the "public interest," as distinguished from the private interests of the utilities, to be "evidenced by the recital in [16 U.S.C. 824(a)] that the scheme of regulation" established by the Act "is necessary in the public interest." 350 U.S. at 355 (quoting 16 U.S.C. 824(a)). The Court therefore directed that the matter be remanded to the Commission for further proceedings, noting that "[w]hether under the facts of this case the contract rate is so low as to have an adverse effect on the public interest is of course a question to be determined in the first instance by the Commission." *Ibid.*

2. a. This case involves the "capacity" market for electricity in New England. In a capacity market, unlike a wholesale energy market, an electricity provider purchases from a generator an option to buy a specific quantity of energy, rather than purchasing the energy itself. Pet. App. 2a. The option mechanism is designed to enable providers to respond adequately to fluctuations in demand and thereby to maintain the reliability of the electric grid. *Ibid.*

Until 1998, the New England electricity market was highly regulated, and generators sold electric energy at wholesale at a price that was based on the cost of production. See *Blumenthal* v. *FERC*, 552 F.3d 875, 878 (D.C. Cir. 2009). In 1998, FERC approved a proposal to

move the New England market toward greater competition. *Ibid.* That action transferred control of the transmission network to an independent system operator (ISO), the ISO New England, and created markets for several different services, including capacity. *Ibid.* Under the new regime, electricity rates—including rates for capacity—generally were set by the market. *Ibid.*

After 1998, the New England capacity market encountered several problems, including an insufficient supply to meet increasing demand. Pet. App. 2a; see *Blumenthal*, 552 F.3d at 878. High-cost generating units were needed to maintain reliability during times of high demand, but the owners of those units found it difficult to earn a profit because their costs usually exceeded the market price during times of normal or low demand. *Ibid.*

b. The Commission instituted proceedings under 16 U.S.C. 824e to revise the New England market rules to address those problems. *Devon Power LLC*, 103 F.E.R.C. ¶ 61,082, at 61,271 (2003), petition for review dismissed, 419 F.3d 1194 (D.C. Cir. 2005). In the proceedings, ISO New England filed a proposal to redesign the wholesale capacity market. Pet. App. 106a. The proposal would have established four separate sub-regions within New England, each of which would have had monthly auctions to establish the price and amount of capacity to be procured for the following month. *Devon Power LLC*, 107 F.E.R.C. ¶ 61,240, at 62,021-62,023 (2004), petition for review dismissed, No. 04-2549 (1st Cir. May 5, 2005). After a hearing, a FERC administrative law judge issued an initial decision that adopted key elements of the proposal. Pet. App. 107a-108a; *Devon Power LLC*, 111 F.E.R.C. ¶ 63,063 (2005).

At the request of opponents of the proposal, the Commission then held an oral argument to consider the issues further. That proceeding showed that New England's generation capacity was "barely adequate," that "deficits [were] predicted in the very near future," that existing generators were losing money, and that new infrastructure was needed soon to avoid reliability problems. Pet. App. 136a-137a. The overwhelming consensus of the parties was that "the status quo presents significant problems that the Commission must address." *Ibid.*

To that end, the Commission established settlement procedures to enable the parties to pursue agreement on an alternative market structure. *Devon Power LLC*, 113 F.E.R.C. ¶ 61,075 (2005). From October 2005 until March 2006, formal settlement negotiations were conducted by representatives of all of the state public-utility regulatory agencies in New England, as well as representatives of transmission owners, generators, power traders and marketers, demand-response and intermittent-resource owners, consumer-owned utility systems, and end users. Pet. App. 139a. Ultimately, a proposed settlement agreement resolving all issues in the proceeding was presented to FERC. *Id.* at 110a. Of the 115 parties participating in the settlement proceedings, only eight parties formally opposed the agreement. *Ibid.*. And only one of those eight objectors—NSTAR Electric and Gas Corporation—actually participates (as a purchaser) in the wholesale capacity market. *Id.* at 121a n.32.

c. The proposed settlement provided for a new long-term structure for the New England capacity market, termed the "forward capacity market." The new market would use annual auctions to establish the price of ca-

pacity for one-year periods beginning three years after each auction. Pet. App. 110a-116a. Instead of establishing pre-defined sub-regions, as the original proposal did, the settlement provided for the creation of separate sub-regions each year based on identifiable transmission constraints that were expected to restrict the delivery of energy. *Id.* at 113a-114a.

Under the settlement, the ISO would conduct the auctions, and the ISO's tariff would document both the obligations of suppliers to deliver capacity and the obligations of load-serving purchasers to pay. J.A. 97-98, 117-118. The auctions would not result in payments directly from purchasers to generators. Instead, the ISO would buy the amount of capacity required to maintain the "installed-capacity requirement" (the capacity necessary to maintain reliability on the grid), and each load-serving entity would then pay for a share of the installed-capacity requirement proportionate to its share of peak load. J.A. 70-71. Utilities would not be required to purchase capacity at the auction price, but could instead choose to "self-supply" by using resources that they owned or for which they separately contracted to meet their capacity obligations. Pet. App. 112a-113a; see J.A. 84-85.

The one-year period beginning June 1, 2010, was the first period for which the forward capacity market auction would procure capacity. Pet. App. 116a. To address the period before that date, the settlement included a transition mechanism, involving a set of fixed transition payments to generators supplying capacity. *Id.* at 116a-117a. As with the annual auctions, obligations of individual load-serving purchasers to cover the cost of the transition payments were calculated based on their share of the peak load. *Id.* at 117a.

3. The Commission approved the proposed settlement. Pet. App. 102a-223a. It concluded that "as a package," the settlement "presents a just and reasonable outcome for this proceeding consistent with the public interest." *Id.* at 103a, 135a-144a. The Commission concluded that the settlement would address "the deficiencies in New England's existing capacity market"—specifically, "the compensation problems faced by generating resources that are needed for reliability but could not obtain sufficient revenue in the markets to continue operation." *Id.* at 135a-136a. And the settlement would "resolve[] all of the outstanding issues in a difficult, contentious and lengthy matter," which had necessitated "difficult compromises among the diverse parties to this proceeding." *Id.* at 139a. The Commission found that the parties objecting to the settlement "would 'be in no worse position under the terms of the settlement than if the case were litigated.'" *Id.* at 141a-142a (quoting *Trailblazer Pipeline Co.*, 87 F.E.R.C. ¶ 61,110, at 61,439 (1999)).

The Commission responded in detail to the issues raised by the parties who opposed the proposed settlement. Pet. App. 144a-218a. For example, while noting that the transition payments were not "ideal as a single market design element," the Commission concluded that, as a component of the larger package embodied in the settlement, the payments were just and reasonable. *Id.* at 151a. In reaching that conclusion, the Commission analyzed record evidence regarding the cost of capacity, finding that the transition payments fell within the "zone of reasonableness" and that those objecting to the payments would not likely achieve a better result through continued litigation. *Id.* at 141a-142a, 152a-158a. The Commission also addressed various issues

relating to the design of the forward capacity market and its auction mechanism. *Id.* at 161a-188a.

Finally, and of particular relevance here, the Commission approved Section 4.C of the proposed settlement. Under the settlement, the rules for conducting the auction would be subject to review by the Commission under the just-and-reasonable standard. Pet. App. 200a. In addition, the results of the auction would be filed with FERC by the New England ISO and would be subject to challenge for a period of 45 days under the just-and-reasonable standard. J.A. 119; Pet. App. 78a, 120a. Under Section 4.C, however, any subsequent challenge to the auction results would be subject to review only under the public-interest standard. *Id.* at 193a-194a. Similarly, any future challenges to the transition payments, which the Commission found in the first instance to be just and reasonable, would be reviewed under the public-interest standard. *Ibid.*

Specifically, Section 4.C provided:

> From the Effective Date, absent the agreement of all Settling Parties to the proposed change, the standard of review for: (i) challenges to the Capacity Clearing Prices derived through the [Forward Capacity Market] and prices resulting from reconfiguration auctions provided for in the Settlement Agreement and in the Market Rules addressing the terms of the Settlement Agreement that are approved or accepted by the FERC pursuant to section 3, and (ii) proposed changes to section 11, Part VIII below (Agreements Regarding Transition Period) and the Market Rules implementing that part, shall be the "public interest" standard of review set forth in *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332 (1956) and *Federal Power Commission*

> *v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956) (the "Mobile-Sierra" doctrine), whether the change is proposed by a Settling Party, a non-Settling Party, or the FERC acting *sua sponte*. This Settlement Agreement does not impose the Mobile-Sierra standard on any provision of this Settlement Agreement or the Market Rules that address the terms of the Settlement Agreement except as expressly provided in this section 4.C.

Pet. App. 193a-194a; J.A. 94.

The Commission stressed that, "even under the 'public interest' standard of review, the Commission retains significant authority to protect non-parties to the settlement from harm." Pet. App. 202a. And the Commission noted that the proposed settlement itself provided for thorough review of final auction prices. *Ibid.* In particular, the settlement provided that ISO New England would make an informational filing before the auction, as well as a filing after the auction containing the results, which would be subject to challenge within 45 days. *Ibid.* The *Mobile-Sierra* provision of Section 4.C did not apply to those filings, which the Commission would review under the ordinary just-and-reasonable standard. *Ibid.*

The Commission concluded that Section 4.C appropriately balanced the need for rate stability with the interests of the diverse entities who would be subject to the forward capacity market. Pet. App. 202a. "Stability is particularly important in this case, which was initiated in part because of the unstable nature of [installed capacity] revenues and the effect that has on generating units, particularly those who are critical to maintaining reliability." *Ibid.* The Commission added that "[t]he Court's statement in *Mobile* that 'all agree . . . [that]

the stability of supply arrangements . . . is essential to the health of the natural gas industry' is no less true with regard to the health of New England's electricity infrastructure." *Id.* at 203a (quoting *Mobile*, 350 U.S. at 344).

The Commission denied petitions for rehearing. Pet. App. 28a-101a. It stated that the tariffs covered by Section 4.C of the settlement were "analogous to contracts," to which *Mobile-Sierra* would apply. *Id.* at 75a-76a. It further pointed out that "the Commission has on many occasions accepted the application of the 'public interest' standard to settlement agreements and contracts setting forth rates." *Id.* at 75a-76a.

4. The court of appeals, while generally rejecting challenges to the Commission's approval of the settlement, sustained the challenge to the Commission's approval of Section 4.C as applied to non-settling parties. Pet. App. 1a-27a. The court stated that, under *Mobile* and *Sierra*, "when the parties to a rate dispute reach a contractual settlement, FERC must enforce the terms of the bargain unless the public interest requires otherwise." *Id.* at 20a. But the court held that the Commission may not approve a settlement agreement applying the *Mobile-Sierra* "public interest" standard to future rate challenges brought by non-contracting (or non-settling) third parties. *Ibid.* In the court's view, the *Mobile-Sierra* doctrine carves out an "exception" to the generally applicable just-and-reasonable standard when a challenge to an existing rate is brought by one of the contracting parties. That doctrine, the court stated, is intended to "make it more difficult for either party to shirk its contractual obligations." *Id.* at 20a, 24a. But the court held that, because a contract cannot bind a nonparty, "when a rate challenge is brought by a non-

contracting third party, the *Mobile-Sierra* doctrine simply does not apply; the proper standard of review remains the 'just and reasonable' standard." *Id.* at 22a. The court concluded that the application of the *Mobile-Sierra* doctrine to future rate challenges by non-settling parties would "deprive[]" them "of their statutory right to have rate challenges adjudicated under the 'just and reasonable' standard." *Ibid.*

5. After the court of appeals issued its decision, this Court decided *Morgan Stanley Capital Group, Inc.* v. *Public Utility District No. 1*, 128 S. Ct. 2733 (2008), in which the Court further addressed the *Mobile-Sierra* doctrine. In *Morgan Stanley*, the Court held that "[t]here is only one statutory standard for assessing wholesale electricity rates, whether set by contract or tariff—the just-and-reasonable standard." *Id.* at 2745. The Court explained that, instead of representing a wholly different standard, the *Mobile-Sierra* "'public interest standard' refers to the differing *application* of the just-and-reasonable standard to contract rates," *id.* at 2740: the *Mobile-Sierra* doctrine, that is, simply "provide[s] a definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context," *id.* at 2746.

6. After *Morgan Stanley* was decided, several parties to this case, including FERC, petitioned for rehearing en banc, contending that the court of appeals' decision was inconsistent with *Morgan Stanley*'s explanation of the *Mobile-Sierra* doctrine. The court of appeals denied the petitions. Pet. App. 245a-248a.

7. On remand, the Commission "approve[d] the settlement conditioned on the settling parties revising the standard of review applicable to non-settling third par-

ties, consistent with the court's decision." *Devon Power, LLC*, 126 F.E.R.C. ¶ 61,027, at ¶ 61,114 (2009).

SUMMARY OF ARGUMENT

The Federal Energy Regulatory Commission acted reasonably and within its statutory authority in approving, as just and reasonable, a comprehensive settlement of disputes concerning the structure of the market for electric capacity in New England. That settlement contained a provision stating that future challenges to certain rates established under the settlement would be governed by the "public interest" standard of review of *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956), and *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956). The court of appeals erred in setting aside the Commission's exercise of discretion in approving this aspect of the settlement, as a result of two fundamental misunderstandings of the *Mobile-Sierra* standard.

First, the court of appeals erroneously believed that the public-interest standard of *Mobile* and *Sierra* is applicable only to challenges to contract rates that are brought by contracting parties. According to the court of appeals, when non-contracting parties challenge a rate, *Mobile-Sierra* "simply does not apply." Pet. App. 22a. That line of reasoning treats *Mobile-Sierra* as a kind of estoppel doctrine, an interpretation that this Court expressly rejected in *Morgan Stanley Capital Group, Inc.* v. *Public Utility District No. 1*, 128 S. Ct. 2733, 2746 (2008). In fact, *Mobile-Sierra* rests on a presumption that rates set out in a freely-negotiated wholesale energy contract are just and reasonable. Nothing in the *Mobile-Sierra* doctrine as elaborated in *Morgan Stanley* limits its applicability to contracting parties, as

opposed to non-contracting third parties. Because it is the rate itself that is presumed just and reasonable, the presumption should apply irrespective of the identity of the party challenging the rate.

Second, the court of appeals believed that, in applying the *Mobile-Sierra* public-interest standard to future rate challenges brought by non-settling parties, the Commission had unlawfully deprived those parties of their statutory right to challenge rates under the just-and-reasonable standard. Pet. App. 22a. But *Morgan Stanley* made clear that the *Mobile-Sierra* public-interest standard is not an exception to the statutory just-and-reasonable standard; it is an application of that standard in the context of rates set by contract. 128 S. Ct. at 2740. The Commission here similarly interpreted the just-and-reasonable standard to involve an inquiry into the public interest in the context of future challenges to rates set under this settlement agreement. As in *Morgan Stanley*, this focus on the public interest did not deprive any party of any statutory right.

This Court has repeatedly held that the Federal Power Act's "just and reasonable" standard leaves the Commission with considerable discretion in setting rates. The Commission properly exercised that discretion in determining that the public-interest standard should be applied here. Although the rates covered by the settlement's public-interest review provision are not themselves contract rates to which the Commission was *required* to apply *Mobile-Sierra*, the Commission carefully reviewed the settlement, and it reasonably determined that the transition payments fell within a zone of reasonableness, that the auction process would produce just and reasonable rates, and that the interest in rate

stability made the application of the public-interest test appropriate.

ARGUMENT

THE FEDERAL ENERGY REGULATORY COMMISSION PERMISSIBLY EXERCISED ITS DISCRETION IN APPROVING THE SETTLEMENT PROVISION AT ISSUE HERE

This Court's decisions in *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956), and *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956)—and most recently *Morgan Stanley Capital Group, Inc.* v. *Public Utility District No. 1*, 128 S. Ct. 2733 (2008)—hold that the Federal Power Act (and parallel provisions of the NGA) require the Commission to apply the "public interest" standard to its review of rates set by private contract. As we explain in Point A, the court of appeals erred in concluding that this statutory mandate, if otherwise applicable, is limited to challenges brought by contracting parties, and does not extend to challenges initiated by third parties, such as consumer groups or state officials. The court of appeals' error on that point is sufficient to require reversal of its ruling on the *Mobile-Sierra* issue.

As we explain in Point B, however, this is not a case in which the Act itself, as construed in *Sierra* and *Morgan Stanley*, required application of the public-interest standard. The rates at issue here are set not by private contract, but pursuant to a tariff that was contained in a contested settlement approved by the Commission. The Commission therefore was not required to prescribe the public-interest standard for future challenges to the rates provided for in that settlement. But the Commission acted within its discretion in choosing to do so. The Commission's determination represents a permissible

and appropriate application of the Act's "just and reasonable" standard in the circumstances of this case, because the manner of setting rates under the contested settlement is analogous to the creation of a private bilateral contract, and because the interests in promoting market stability and assuring an adequate supply of energy which underlie the *Mobile-Sierra* requirement are also present here. And once having decided to approve use of the public-interest standard, the Commission acted permissibly and appropriately in approving the application of that standard to future challenges by third parties (including the non-settling parties here), just as the Commission would have done if required to apply the *Mobile-Sierra* standard.

A. The *Mobile-Sierra* Doctrine Is Fully Applicable To Third-Party Challenges To Contract Rates And Terms

The court of appeals erred in holding that the *Mobile-Sierra* "public interest" standard applies only to the contracting parties and not to third parties challenging a transaction. In the court's view, "the *Mobile-Sierra* doctrine is designed to ensure contract stability *as between the contracting parties*—*i.e.* to make it more difficult for either party to shirk its contractual obligations." Pet. App. 24a. By contrast, the court concluded, "when a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply." *Id.* at 22a. That is incorrect. Under *Mobile* and *Sierra*, a contractually negotiated rate is presumed just and reasonable, and no basis exists for limiting the application of that presumption to challenges brought by the contracting parties, as opposed to other persons who might challenge the contract rate.

1. The court of appeals' reasoning echoes the argument embraced by the Ninth Circuit but rejected by this Court in *Morgan Stanley*—that *Mobile-Sierra* is "the equivalent of an estoppel doctrine." 128 S. Ct. at 2746 (quoting David G. Tewksbury & Stephanie S. Lim, *Applying the* Mobile-Sierra *Doctrine to Market-Based Rate Contracts*, 26 Energy L.J. 437, 458 (2005)). *Morgan Stanley* held that *Sierra* does not rest on the premise that the Commission is estopped from disapproving an agreed-upon rate after once approving it as just and reasonable. Neither does *Sierra* rest on the notion that the contracting parties are estopped from challenging a rate to which they have agreed. *Sierra* instead reflects a "presum[ption] that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law." *Id.* at 2737. *Sierra* "was grounded in the commonsense notion that 'in wholesale markets, the party charging the rate and the party charged [are] often sophisticated businesses enjoying presumptively equal bargaining power, who could be expected to negotiate a "just and reasonable" rate as between the two of them.'" *Id.* at 2746 (quoting *Verizon Commc'ns Inc.* v. *FCC*, 535 U.S. 467, 479 (2002)). Nothing in *Mobile* and *Sierra*, as interpreted in *Morgan Stanley*, limits the applicability of that presumption to situations in which a challenge is brought by the contracting parties. The negotiation between these parties creates the basis for presuming the contract rate to be just and reasonable. But once the presumption comes into effect, it should apply regardless of the identity of the party challenging the rate. Whether a contracting party or a third party or no one at all files a complaint, the question for FERC, acting under 16 U.S.C. 824e, is

always the same: whether the rate in question continues to be just and reasonable.

The oddity of exempting third-party challenges from the *Mobile-Sierra* "public interest" standard would be particularly great, given that the very point of that standard is to protect third parties. The *Mobile-Sierra* standard permits the Commission to modify a contract rate in precisely those circumstances in which third parties—*i.e.*, members of the "public"—are seriously harmed by a contractually specified rate. Under *Mobile-Sierra*, "only when the mutually agreed-upon contract rate seriously harms the consuming public may the Commission declare it not to be just and reasonable." *Morgan Stanley*, 128 S. Ct. at 2746; see *Verizon Commc'ns*, 535 U.S. at 479 (When a buyer and a seller agree upon a rate, "the principal regulatory responsibility [is] not to relieve a contracting party of an unreasonable rate, * * * but to protect against potential discrimination by favorable contract rates between allied businesses to the detriment of *other* wholesale customers.") (emphasis added). The court of appeals' decision thus divorced the standard's application from its most essential purpose.

2. In addition, the court of appeals established prerequisites to applying *Sierra* similar to the ones that this Court rejected in *Morgan Stanley*. In that case, the Court rejected the contention that *Sierra* was inapplicable to contracts that had not previously been subject to just-and-reasonable rate review by the Commission. The Court explained that the "definition of what it means for a rate to satisfy the just-and-reasonable standard" in the contract context is "a definition that applies regardless of when the contract is reviewed"; accordingly, the application of *Sierra* does not depend on when

a contract rate is challenged. 128 S. Ct. at 2746. For a similar reason—that the definition of what it means for a contract rate to be just and reasonable remains the same—neither does the applicability of *Sierra* depend on who might initiate such a challenge.

The Court in *Morgan Stanley* also rejected the suggestion that the *Mobile-Sierra* presumption applies differently depending upon whether a challenge is brought by a buyer or a seller. Instead, the Court held that the public-interest standards of "unequivocal public necessity" and "extraordinary circumstances" that apply when sellers complain that rates are too low have equal application when consumers complain that rates are too high. 128 S. Ct. at 2748 (quoting *Permian Basin Area Rate Cases*, 390 U.S. 747, 822 (1968), and *Arkansas La. Gas Co.* v. *Hall*, 453 U.S. 571, 582 (1981)). In either situation, the Court explained, "[t]he contract rate must seriously harm the public interest" before it may be set aside. *Id.* at 2747; see *id.* at 2750 (rate may be set aside only in case of "unequivocal public necessity"); *ibid.* (relief available only where "increase is so great" that rates "impose an excessive burden on consumers or otherwise seriously harm the public interest"); see also *Potomac Elec. Power Co.* v. *FERC*, 210 F.3d 403, 411 (D.C. Cir. 2000) (*PEPCO*). Just as there is no basis for treating challenges brought by buyers more favorably under *Mobile-Sierra*'s "public interest" standard than challenges brought by sellers, so too there is no basis for treating challenges brought by non-parties more favorably still by exempting them from the application of the *Mobile-Sierra* framework altogether.

3. Under the court of appeals' reasoning, the Commission would use a different standard when it investigates a rate on its own initiative under 16 U.S.C. 824e

than when it acts on a complaint filed by a non-contracting party. The court of appeals has recognized that contracting parties can bind the Commission, acting under 16 U.S.C. 824e, to the *Mobile-Sierra* public-interest standard. See *Papago Tribal Util. Auth.* v. *FERC*, 723 F.2d 950, 953 (D.C. Cir. 1983) (Scalia, J.) ("[B]y broad waiver, the parties may eliminate both the utility's right to make immediately effective rate changes under [Section 824d] and the Commission's power to impose changes under [Section 824e], except the indefeasible right of the Commission under [Section 824e] to replace rates that are contrary to the public interest."), cert. denied, 467 U.S. 1241 (1984); see *Maine Public Utils. Comm'n* v. *FERC*, 454 F.3d 278, 283 (D.C. Cir. 2006). Commission-initated investigations of contract rates are uncommon, but not unprecedented. See, *e.g.*, *Wisconsin Pub. Power Inc.* v. *FERC*, 493 F.3d 239, 253-254, 272-273 (D.C. Cir. 2007); *Boston Edison Co.* v. *FERC*, 233 F.3d 60, 63 (1st Cir. 2000); *Northeast Utils. Serv. Co.* v. *FERC*, 993 F.2d 937, 943, 960 (1st Cir. 1993); *Borough of Chambersburg* v. *FERC*, 580 F.2d 573, 574 (D.C. Cir. 1978); *Public Serv. Co. of Ind., Inc.* v. *FERC*, 575 F.2d 1204, 1209 (7th Cir. 1978). Under the court of appeals' decision, the rates at issue in such cases would be subject to a different standard of review if they were challenged in complaints by a third party—such as a consumer group or state regulatory agency—rather than in a proceeding initiated by the Commission itself. That result makes little sense, and it finds no support in the FPA or this Court's cases.

4. Finally, the third-party exception created by the court of appeals would seriously undermine the purposes of the *Mobile-Sierra* rule. The FPA, as interpreted in *Sierra*, "recognizes that contract stability ulti-

mately benefits consumers" by encouraging investment, "which is why [the Act] permits rates to be set by contract and not just by tariff." *Morgan Stanley*, 128 S. Ct. at 2749; see *Mobile*, 350 U.S. at 344 ("By preserving the integrity of contracts, [the NGA] promotes the stability of supply arrangements which all agree is essential to the health of the natural gas industry."). That is especially so here: as the Commission explained, "[s]tability is particularly important in this case, which was initiated in part because of the unstable nature of [installed capacity] revenues and the effect that has on generating units, particularly those who are critical to maintaining reliability." Pet. App. 202a. If contract rates could readily be set aside at the behest of any non-contracting party, suppliers and customers would not have the assurance of stability that the *Mobile-Sierra* rule is intended to provide.

B. Although Not Required By The Act To Do So, The Commission Permissibly Chose To Approve A "Public Interest" Standard Of Review For Future Challenges Under The Contested Settlement

The court of appeals' error in creating a third-party exception to the *Mobile-Sierra* presumption is a sufficient basis for reversing its judgment. Respondents have contended, however, that the court of appeals reached the right result because the rates at issue in this case are not set by contract, and the *Mobile-Sierra* presumption therefore does not apply at all. Connecticut Att'y Gen. Br. in Opp. 10-12. Respondents are correct that the Commission's approval of Section 4.C of the proposed settlement in this case did not rest on a direct application of *Sierra* and the public-interest standard it construed the Act to require in the context of rates set

by private contract. But respondents are wrong to think that this fact resolves the case in their favor. The Commission exercised its discretion in this case to approve the proposed settlement—including Section 4.C—under the FPA's general requirement that rates be just and reasonable. The Commission effectively determined that applying the just-and-reasonable standard in the context of future challenges to rates set under this settlement meant inquiring into the public interest, much as *Sierra* had determined that it did in the context of a bilateral private contract. And because the public-interest test provided for in the Commission's action simply implements the statutory just-and-reasonable standard, its application does not deprive any party—settling or non-settling, contracting or non-contracting—of the statutory right to a just and reasonable rate.

In approving the comprehensive settlement of the disputes concerning the structure of the New England capacity market, the Commission specified the standard of review that it will apply to two kinds of future complaints: complaints about the prices set by the capacity auctions and complaints about the transition payments specified in the settlement. Pet. App. 193a-194a. Section 4.C of the settlement provides that those complaints will be reviewed under "the 'public interest' standard of review set forth in" *Mobile* and *Sierra*, "whether the change is proposed by a Settling Party, a non-Settling Party, or the FERC acting *sua sponte*." *Id.* at 193a. Because such complaints would invoke the Commission's authority under 16 U.S.C. 824e(a) to set aside rates that are "unjust, unreasonable, unduly discriminatory or preferential," as well as its authority under 16 U.S.C. 824d(a) to ensure that "[a]ll rates and charges * * * shall be just and reasonable," FERC's approval of Sec-

tion 4.C represents an interpretation and application of Sections 824d and 824e. That interpretation was reached in a formal adjudication, and it is entitled to deference under *Chevron U.S.A. Inc.* v. *NRDC*, 467 U.S. 837 (1984). See *United States* v. *Mead Corp.*, 533 U.S. 218, 229 (2001).

1. Congress has not specified the precise standard of review that FERC must apply to complaints under Sections 824d and 824e

Neither Section 824d nor Section 824e speaks directly "to the precise question at issue" in this case, which concerns the standard of review that FERC must apply to future complaints about the capacity-auction results or transition payments established by the settlement. *Chevron*, 467 U.S. at 842. The FPA requires that rates be just and reasonable, but it does not specify the manner in which that general formulation will be implemented in any particular context. Under the "just and reasonable" standard, the Commission is not "bound to any one ratemaking formula." *Morgan Stanley*, 128 S. Ct. at 2738; accord *Permian Basin Area Rate Cases*, 390 U.S. at 767; *Montana-Dakota Utils. Co.* v. *Northwestern Pub. Serv. Co.*, 341 U.S. 246, 251 (1951); *FPC* v. *Hope Natural Gas Co.*, 320 U.S. 591, 602 (1944). Instead, because "[t]he statutory requirement that rates be 'just and reasonable' is obviously incapable of precise judicial definition," the Court "afford[s] great deference to the Commission in its rate decisions." *Morgan Stanley*, 128 S. Ct. at 2738; see *Global Crossing Telecomms., Inc.* v. *Metrophones Telecomms., Inc.*, 550 U.S. 45, 58 (2007) (applying *Chevron* to the Federal Communications Commission's interpretation of 47 U.S.C. 201(b), which prohibits "unjust or unreasonable" practices); *Capital Net-*

work Sys., Inc. v. *FCC*, 28 F.3d 201, 204 (D.C. Cir. 1994) (noting that "'just,' 'unjust,' 'reasonable,' and 'unreasonable' are ambiguous statutory terms"). FERC's interpretation must therefore be upheld so long as it represents "a permissible construction of the statute." *Chevron*, 467 U.S. at 843.

2. The "public interest" standard approved by FERC in the circumstances of this case is consistent with the statutory "just and reasonable" standard

Section 4.C of the settlement provides that the Commission shall review certain kinds of future complaints under "the 'public interest' standard of review set forth in" *Mobile* and *Sierra*. Pet. App. 193a-194a. Under that standard, a rate may be set aside only if it "adversely affect[s] the public interest—as where it might impair the financial ability of the public utility to continue its service, cast upon other customers an excessive burden, or be unduly discriminatory." *Sierra*, 350 U.S. at 355. The court of appeals held that, in approving that provision, the Commission had deprived the non-settling parties "of their statutory right to challenge rates under the 'just and reasonable' standard." Pet. App. 19a; see *id.* at 2a. In the court's view, the public-interest standard is an "exception" to just-and-reasonable rate review that is applicable only to relations between the contracting parties. *Id.* at 20a. Thus, the court reasoned, "when a rate challenge is brought by a non-contracting third party," that standard "simply does not apply; the proper standard of review remains the 'just and reasonable' standard" of Section 824e. *Id.* at 22a. The reasoning of the court of appeals rests on a misunderstanding of the relationship between the *Mobile-Sierra* "public interest"

standard and the ordinary "just and reasonable" standard.

In *Morgan Stanley*, this Court emphatically rejected, as "obviously indefensible," the "proposition that a standard different from the statutory just-and-reasonable standard applies to contract rates." 128 S. Ct. at 2740. Instead, "[t]here is only one statutory standard for assessing wholesale electricity rates, whether set by contract or tariff—the just-and-reasonable standard." *Id.* at 2745. The "public interest" test applied under *Mobile* and *Sierra* is not a different standard; rather, "the term * * * refers to the differing *application* of the just-and-reasonable standard to contract rates." *Id.* at 2740; see also *id.* at 2746 (observing that "*Sierra* thus provided a definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context.").

As this understanding of the relationship between the just-and-reasonable standard and the public-interest test suggests, no impermeable wall separates the two formulations or the Commission's actions under them. For one thing, application of the public-interest standard itself calls for the exercise of judgment and discretion by the Commission. The Court recognized as much in *Sierra* when, upon concluding that the Act required application of the "public interest" standard to determine whether contract rates were just and reasonable, the Court held that the question whether the rates at issue were contrary to the public interest "is of course a question to be determined in the first instance by the Commission." 350 U.S. at 355; see *FCC* v. *RCA Commc'ns, Inc.*, 346 U.S. 86, 90 (1953) (describing the "public interest, convenience, or necessity" standard of the Radio Act of 1927, ch. 169, § 4, 44 Stat. 1163, as

"[n]ot a standard that lends itself to application with exactitude," but one that "leaves wide discretion and calls for imaginative interpretation"); *Mistretta* v. *United States*, 488 U.S. 361, 416 (1989) (Scalia, J., dissenting) (pointing to the "public interest" standard as an example of the breadth of scope for permissible delegation). The Commission's actions under *Mobile* and *Sierra* thus can run a gamut, rather than striking in each case the identical note.

At the same time, the Commission may act under even the ordinary just-and-reasonable standard in ways that reflect the premises of the *Mobile-Sierra* approach. In determining just and reasonable rates, FERC may recognize, for example, that "stability ultimately benefits consumers, even if short-term rates for a subset of the public might be high by historical standards." *Morgan Stanley*, 128 S. Ct. at 2749. Similarly, Commission precedent requires most rate challengers to show changed circumstances in order to obtain a rate change, even under the general just-and-reasonable standard. See, *e.g.*, *Dynegy Moss Landing, LLC*, 123 F.E.R.C. ¶ 61,280, at 62,724 (2008); *Northern Va. Elec. Coop., Inc.*, 116 F.E.R.C. ¶ 61,173, at 61,741. In other words, although the public-interest test imposes a more demanding burden on those challenging rates than does the ordinary just-and-reasonable standard, see *Morgan Stanley*, 128 S. Ct. at 2746, the precise degree of difference between the two is committed to the Commission's discretion and may vary depending on the context.

Under *Morgan Stanley*, then, the public-interest test is simply a rigorous application of the statutory "just and reasonable" standard. Rather than being an extra-statutory test, separate and apart from the "just and reasonable" standard, the public-interest test repre-

sents a set of points on a still broader continuum of approaches to the requirement that rates be just and reasonable. In cases such as *Sierra* and *Morgan Stanley*, where rates are set by private contract, the Court has construed the Act to require application of the public-interest standard. But those rulings do not bar the Commission from applying a similar standard in other circumstances as a matter of administrative discretion, in cases in which the Commission determines that considerations relevant to what is "just and reasonable" support that approach. The court of appeals therefore erred in holding that the Act's "just and reasonable" standard itself precluded FERC from applying the public-interest standard to third parties by approving Section 4.C of the settlement.

3. Although FERC was not required to adopt the "public interest" standard of review in this case, it had discretion to do so

In *Morgan Stanley*, this Court held that the Commission is "*required* * * * to apply the *Mobile-Sierra* presumption" when it evaluates "a contract rate." 128 S. Ct. at 2745. Section 4.C of the settlement is not itself part of a contract governed by the *Mobile-Sierra* presumption, nor does the section concern the review of rates that are set by such contracts. The Commission therefore was not required to approve that provision's adoption of the public-interest standard of review. But the Commission had discretion to do so.

a. Under *Mobile* and *Sierra*, the Commission is required to apply the public-interest standard in its review of rates set by contracts that are freely negotiated between the contracting parties. See *Morgan Stanley*, 128 S. Ct. at 2737 (*Mobile-Sierra* presumption applies to

"a freely negotiated wholesale-energy contract"); *id.* at 2746 (*Mobile-Sierra* applies to a "mutually agreed-upon contract rate"). As previously noted, the *Mobile-Sierra* doctrine rests on the premise that "the contract rates are the product of fair, arms-length negotiations." *Id.* at 2750. When that condition is satisfied, the deferential public-interest standard is justified by "the commonsense notion that '[i]n wholesale markets, the party charging the rate and the party charged [are] often sophisticated businesses enjoying presumptively equal bargaining power, who could be expected to negotiate a "just and reasonable" rate as between the two of them.'" *Id.* at 2746 (quoting *Verizon Commcn's*, 535 U.S. at 479) (brackets in original).

Accordingly, in *Morgan Stanley*, as in other cases in which this Court has applied the *Mobile-Sierra* doctrine, the contracts at issue were freely negotiated wholesale energy contracts. See, *e.g.*, 128 S. Ct. at 2743; *Mobile*, 350 U.S. at 333-334 (long-term bilateral contract for the sale of natural gas between a natural gas utility and a distribution company); *Sierra*, 350 U.S. at 351-352 (long-term bilateral power-purchase contract between a distribution company and an electric utility); see also *Boston Edison Co.*, 233 F.3d at 61 (contracts between utilities allocating the output of a nuclear power station); *PEPCO*, 210 F.3d at 404 (long-term power supply agreement between utilities); *Northeast Utils. Serv. Co.*, 993 F.2d at 960 (power contract between utilities). That context creates a presumption that the negotiated rate is just and reasonable, and therefore the Commission must apply the deferential public-interest standard.

b. By contrast, the statutory *Mobile-Sierra* presumption does not apply, of its own force, when the parties have not agreed to set rates wholly by private con-

tract. See *Morgan Stanley*, 128 S. Ct. at 2750. For that reason, neither of the two types of rates to which Section 4.C of the settlement applies—the rates resulting from the capacity auctions and the transition payments established by the settlement—is subject to the statutory *Mobile-Sierra* presumption, and the Commission was not *required* to apply the public-interest standard to its review of those rates.

The results of the capacity auctions, although possessing certain characteristics of contracts, do not constitute contracts between buyers and sellers. Under the auction rules as established in the settlement agreement, the obligations of suppliers to deliver capacity and the obligations of purchasers of capacity to make payments are documented in the ISO's tariff. J.A. 117. The auctions result in binding obligations by sellers to offer capacity during the relevant commitment period. J.A. 143. The auctions also result in a commitment by the ISO to buy the amount of capacity required to maintain the installed-capacity requirement—and, by extension, by each load-serving entity participating in the auction to pay for a share of the installed-capacity requirement proportionate to its share of peak load. J.A. 71.[1] But the auction results are not recorded in separate agreements between a particular generator and a particular purchasing entity—or even separate agreements between any of those participants and the ISO, the facilitating entity at the middle of the market. Likewise, the consequences of default are specified not in an agreement between participants in the auction but in a tariff filed

[1] Load-serving utilities are not required to participate in the capacity auctions. They may instead "self-supply," obtaining the requisite capacity by using resources that they own or for which they have separately contracted. Pet. App. 112a-113a; see J.A. 84-85.

by the ISO. J.A. 117. Thus, the prices to be set by the auction will not reflect the kind of negotiated agreement between buyer and seller to which *Sierra* and *Morgan Stanley* require the Commission to apply the public-interest standard.

The transition payments are also not the product of a contract for which the Act requires *Mobile-Sierra* public-interest review. The payments are specified in the settlement. J.A. 163-170. Although the settlement represented an agreement among the signators, it was not a private contract of the sort at issue in *Mobile*, *Sierra*, and *Morgan Stanley*. It was, rather, the resolution of a disputed proceeding before the Commission, and it was submitted to the Commission for its approval under longstanding regulations governing settlements of such disputes. Moreover, the proposed settlement was contested by certain parties to the proceeding—a distribution company, several state entities, and representatives of large end-users. Pet. App. 121a & n.32. The transition payments apply to all suppliers and purchasers of capacity—including the contesting parties and all future entrants into the market—not just to the settling parties. As to these other participants, the transition payments do not resemble contractually negotiated rates at all.

c. In its order approving the settlement, FERC correctly recognized that it was not compelled by the *Mobile-Sierra* doctrine to apply the public-interest standard of review to the rates specified in Section 4.C. Instead, the Commission stated that it had "broad authority and discretion * * * to address contested settlements," Pet. App. 133a, and explained that it was approving the settlement after finding that the proposal was "consistent with the public interest," *id.* at 135a, and

that it "achieve[d] an overall just and reasonable result," *id.* at 141a-142a. With respect to Section 4.C in particular, the Commission stated that application of the public-interest standard of review to future challenges to rates would be "fully consistent with current Commission policy." *Id.* at 201a; see *ibid.* ("[W]e find this *Mobile-Sierra* provision reasonable."). In the Commission's view, Section 4.C "appropriately balances the need for rate stability and the interests of the diverse entities who will be subject to" the settlement. *Id.* at 202a.

The public-interest standard of review is simply one application of the more general just-and-reasonable standard in the Act, and the Commission's exercise of its discretion to approve the application of the public-interest standard, based on the totality of the circumstances of the proceeding, was permitted by 16 U.S.C. 824d and 824e. As explained below, that choice was also a reasonable one.

C. The Commission Acted Reasonably In Approving The Settlement

Because "Congress has not directly addressed the precise question at issue in this case," FERC's decision must be upheld as long as it "is based on a permissible construction of the statute." *Chevron*, 467 U.S. at 843. The Commission's approval of Section 4.C of the settlement represents a reasonable implementation of the FPA's requirement that rates be just and reasonable.

1. FERC found the settlement as a whole to be just and reasonable

a. The Commission recognized in its order that it may approve a contested settlement only upon making an independent determination that the settlement will establish just and reasonable rates. Pet. App. 133a

("Courts have confirmed the Commission's authority to approve contested settlements, so long as the proposal will establish just and reasonable rates."). That observation was consistent with this Court's decision in *Mobil Oil Corp.* v. *FPC*, 417 U.S. 283 (1974), which held that the Commission has the authority "to adopt as a rate order a settlement proposal that lacks unanimous agreement of the parties to the proceeding," *id.* at 312, but that such a proposal may only be "adopted as a resolution *on the merits* if the [Commission] makes an independent finding supported by 'substantial evidence on the record as a whole' that the proposal will establish 'just and reasonable' rates," *id.* at 314 (quoting *Placid Oil Co.* v. *FPC*, 483 F.2d 880, 893 (5th Cir. 1973), aff'd *sub nom. Mobil Oil Corp.* v. *FPC*, 417 U.S. 283 (1974)). See *Tejas Power Corp.* v. *FERC*, 908 F.2d 998, 1003 (D.C. Cir. 1990); *New Orleans Pub. Serv., Inc.* v. *FERC*, 659 F.2d 509, 511-512 (5th Cir. 1981); *Pennsylvania Gas & Water Co.* v. *FPC*, 463 F.2d 1242, 1249-1250 (D.C. Cir. 1972). The Commission's regulation on contested settlements, 18 C.F.R. 385.602(h)—which the Commission applied in this case, Pet. App. 133a—"effectively codifies the principles articulated in *Mobil Oil*." *Laclede Gas Co.* v. *FERC*, 997 F.2d 936, 944 (D.C. Cir. 1993). Under that regulation, "that the proposal is a settlement does not 'establish without more the justness and reasonableness of its terms.'" *Tejas Power Corp.*, 908 F.2d at 1003 (quoting *Mobil Oil*, 417 U.S. at 312-313). Instead, "a settlement proposal in a [contested] proceeding like the instant one is in the nature of a motion for summary judgment, and the agency may reach such a judgment on such terms as it deems fair from the evidence before it." *Consolidated Gas Supply Corp.* v. *FERC*, 606 F.2d 323, 330 (D.C. Cir. 1979), cert. denied, 444 U.S. 1073

(1980); see *Pennsylvania Gas & Water Co.*, 463 F.2d at 1246.

The Commission's review of contested settlements is guided by its decision in *Trailblazer Pipeline Co.*, 85 F.E.R.C. ¶ 61,345 (1998), order on denial of reh'g, 87 F.E.R.C. ¶ 61,110 (1999). In *Trailblazer*, the Commission reviewed the case law regarding contested settlements, and it set out a framework to guide its discretion in addressing such settlements. *Id.* at 62,339-62,345. Under that framework, the Commission first determines "whether the settlement presents an acceptable outcome for the case that is consistent with the public interest." *Id.* at 62,341; see Pet. App. 134a. If the Commission answers that question affirmatively, it will then choose an approach to address the contested issues. *Trailblazer*, 85 F.E.R.C. at 62,342; Pet. App. 134a. Under one such approach—the approach employed here, *Id.* at 140a-141a—the Commission "approve[s] a contested settlement as a package" if it finds that it "provides an overall just and reasonable result," 85 F.E.R.C. at 62,342.

b. The Commission correctly applied the *Trailblazer* approach in this case when it approved the proposed settlement after concluding that it was "consistent with the public interest," Pet. App. 135a, and that, "as a package, [it] achieve[d] an overall just and reasonable result," *id.* at 141a-142a. In deciding to consider the settlement as a package, the Commission noted its "several complex and interrelated features" and concluded that "altering any of those features will have consequences for other portions of the settlement." *Id.* at 141a; see *id.* at 140a (noting that the settling parties had requested that the agreement be considered as a package). Indeed, the proposed settlement itself provided that it

would be effective only if it was approved "in its entirety without modifications or conditions." J.A. 92.

The Commission found that the settlement would "resolve the deficiencies in New England's capacity market"—specifically, "the compensation problems faced by generating resources that are needed for reliability but could not obtain sufficient revenue in the markets to continue operation." Pet. App. 135a-136a. The settlement would, moreover, "resolve[] all of the outstanding issues in a difficult, contentious and lengthy matter," involving "difficult compromises among the diverse parties to this proceeding." *Id.* at 139a.

The Commission also took into account "the level of support for the Settlement Agreement"—namely, that the agreement "was either supported or not opposed by 107 of the 115 parties in the proceeding," a level of support that the Commission regarded as "'quite extraordinary.'" Pet. App. 143a-144a (quoting *Devon Power LLC*, 115 F.E.R.C. ¶ 63,013, at 65,075 (2006)). Although acknowledging that this factor "is not dispositive," the Commission reasonably determined that it is entitled to some weight. *Id.* at 143a; see *NorAm Gas Transmission Co.* v. *FERC*, 148 F.3d 1158, 1165 (D.C. Cir. 1998) ("[T]he Commission is clearly entitled to give weight to the support of customers when deciding whether to approve a settlement offer."). Similarly, the Commission noted that the settlement included many of the market-design features that the States in the region had advocated. Pet. App. 137a.

Finally, to ensure the justness and reasonableness of the settlement as a package, the Commission responded in detail to the issues raised by the objectors. Pet. App. 144a-218a. In particular, the Commission addressed issues regarding the transition mechanism, *id.* at 151a-

160a, and design elements of the forward capacity market, *id.* at 161a-188a. Additionally, the Commission considered the proposed "public interest" review provision in Section 4.C. *Id.* at 200a-203a. It emphasized that the provision "will only apply to (1) the final clearing prices in the [forward capacity auction] and any reconfiguration auctions permitted under the market rules, and (2) the transition mechanism." *Id.* at 200a; see *id.* at 75a. As explained below, the Commission reasonably evaluated both components of that provision and determined that it was just and reasonable.

2. Application of the public-interest standard to challenges to the auction results is reasonable

The Commission reasonably approved Section 4.C's application of the public-interest standard to any challenges brought after an initial 45-day period to the prices set by forward capacity auctions. Although these auctions will not result in contracts between buyers and sellers, see pp. 30-31, *supra*, they share with freely negotiated contracts certain market-based features that render use of the public-interest standard appropriate. The Commission carefully reviewed the design of the proposed auctions and found that it would produce prices that are just and reasonable. Pet. App. 161a-193a; see *id.* at 142a ("[T]he key price-determining parameters of the [forward capacity market] descending clock auction * * * are appropriate and adequately supported in the record."). In other contexts, courts of appeals have recognized that rates set by a market are consistent with the requirements of the FPA and cognate statutes. "[W]hen there is a competitive market the FERC may rely upon market-based prices in lieu of cost-of-service regulation to assure a 'just and

reasonable' result." *Elizabethtown Gas Co.* v. *FERC*, 10 F.3d 866, 870 (D.C. Cir. 1993); see *Louisiana Energy & Power Auth.* v. *FERC*, 141 F.3d 364, 365 (D.C. Cir. 1998); *Cajun Elec. Power Coop., Inc.* v. *FERC*, 28 F.3d 173, 176, 179, 180 (D.C. Cir. 1994); *Tejas Power Corp.*, 908 F.2d at 1004. "[I]n a competitive market, where neither buyer nor seller has significant market power," courts have held that "it is rational to assume that the terms of their voluntary exchange are reasonable, and specifically to infer that the price is close to marginal cost, such that the seller makes only a normal return on its investment." *California ex rel. Lockyer* v. *FERC*, 383 F.3d 1006, 1013 (9th Cir. 2004) (quoting *Tejas Power Corp.*, 908 F.2d at 1004), cert. denied, 127 S. Ct. 2972 (2007). Accordingly, the Commission reasonably could presume that the parties to the New England capacity auctions would arrive at just and reasonable rates. See *Morgan Stanley*, 128 S. Ct. at 2746.

The appropriateness of this presumption is enhanced by terms of the settlement that provide for ongoing monitoring of the auction process by the Commission. The settlement agreement requires that ISO New England make an informational filing with the Commission before each auction. Pet. App. 202a. In addition, the results will be filed with the Commission after the auction, and these will be subject to challenge for a period of 45 days. *Ibid.*; J.A. 119. The public-interest provision of Section 4.C does not apply to either of those filings, and the Commission can review them under the ordinary just-and-reasonable standard.

Section 4.C also "does not apply to the market rules that will be developed and filed with the Commission under the Settlement Agreement." *Id.* at 200a. Accordingly, should any party develop reason to believe that

the auction rules are not just and reasonable, the Commission can alter the rules as appropriate, entirely unrestricted by Section 4.C. See *id.* at 78a ("These provisions also address concerns that the [forward capacity market] design is untested; these regular filings will reveal any unanticipated problems with that design, giving the parties an opportunity to address them under the just and reasonable standard.").

In addition, the Commission determined that application of the public-interest standard to auction results would promote an important interest in rate stability. As the Commission explained, "[s]tability is particularly important in this case, which was initiated in part because of the unstable nature of [capacity] revenues and the effect that has on generating units, particularly those who are critical to maintaining reliability." Pet. App. 202a; see *id.* at 78a ("[P]rice certainty is important to ensure that the [forward capacity market] achieves its goals of attracting and retaining generators needed for reliability."). Quoting this Court's observation in *Mobile* that "the stability of supply arrangements . . . is essential to the health of the natural gas industry," the Commission found that that statement "is no less true with regard to the health of New England's electricity infrastructure." *Id.* at 204a (quoting *Mobile*, 350 U.S. at 344); see *Morgan Stanley*, 128 S. Ct. at 2749 (describing the *Mobile-Sierra* public-interest standard as "a key source of stability"). That finding, coupled with the presumptively just and reasonable nature of the auction prices, amply supports the Commission's exercise of discretion to assess challenges to rates set by auction under the public-interest standard, after an initial 45-day period during which those rates may be challenged under ordinary just-and-reasonable principles.

3. *Application of the public-interest standard to challenges to the transition payments is reasonable*

The Commission also acted reasonably in approving application of the public-interest standard to any future challenges to the transition payments, which were set forth in the settlement agreement. In approving the settlement, FERC reviewed the transition payments specified and found them to be just and reasonable, Pet. App. 144a-161a, a finding that the court of appeals upheld, *id.* at 8a-19a. The Commission could reasonably determine that, given the interest in the stability of the settlement and its provision for prompt transition to capacity auctions, *id.* at 202a-203a, a party seeking to alter the transition payments should have to show that they were impairing the public interest. Cf. *Horne* v. *Flores*, No. 08-289 (June 25, 2009), slip op. 10 (explaining that modification of an order entered by a court is appropriate under Federal Rule of Civil Procedure 60(b)(5) "if 'a significant change either in factual conditions or in law' renders continued enforcement 'detrimental to the public interest'") (quoting *Rufo* v. *Inmates of Suffolk County Jail*, 502 U.S. 367, 384 (1992)).

Significantly, the transition payments last only for a limited time, with the final payment to be made in May 2010. J.A. 163. The short duration of the payment regime makes it unlikely that the transition payments will become unjust or unreasonable. Indeed, the parties challenging the settlement have not indicated that they are likely to bring a renewed challenge to the transition payments. And they surely have not shown that circumstances in the New England capacity market are likely to change in a way that would undermine FERC's initial determination that the transition payments are just and reasonable.

CONCLUSION

The judgment of the court of appeals should be reversed insofar as it granted the petitions for review.

Respectfully submitted.

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APPENDIX

1. 16 U.S.C. 824 provides:

Declaration of policy; application of subchapter

(a) Federal regulation of transmission and sale of electric energy

It is declared that the business of transmitting and selling electric energy for ultimate distribution to the public is affected with a public interest, and that Federal regulation of matters relating to generation to the extent provided in this subchapter and subchapter III of this chapter and of that part of such business which consists of the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce is necessary in the public interest, such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States.

(b) Use or sale of electric energy in interstate commerce

(1) The provisions of this subchapter shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce, but except as provided in paragraph (2) shall not apply to any other sale of electric energy or deprive a State or State commission of its lawful authority now exercised over the exportation of hydroelectric energy which is transmitted across a State line. The Commission shall have jurisdiction over all facilities for such transmission or sale of electric energy, but shall not have jurisdiction, except as specifically provided in this subchapter and subchapter III of this chapter, over facilities used for the generation of electric en-

ergy or over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce, or over facilities for the transmission of electric energy consumed wholly by the transmitter.

(2) Notwithstanding subsection (f) of this section, the provisions of sections 824b(a)(2), 824e(e), 824i, 824j, 824j-1, 824k, 824*o*, 824p, 824q, 824r, 824s, 824t, 824u, and 824v shall apply to the entities described in such provisions, and such entities shall be subject to the jurisdiction of the Commission for purposes of carrying out such provisions and for purposes of applying the enforcement authorities of this chapter with respect to such provisions. Compliance with any order or rule of the Commission under the provisions of section 824b(a)(2), 824e(e), 824i, 824j, 824j-1, 824k, 824*o*, 824p, 824q, 824r, 824s, 824t, 824u, or 824v, shall not make an electric utility or other entity subject to the jurisdiction of the Commission for any purposes other than the purposes specified in the preceding sentence.

(c) Electric energy in interstate commerce

For the purpose of this subchapter, electric energy shall be held to be transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof; but only insofar as such transmission takes place within the United States.

(d) "Sale of electric energy at wholesale" defined

The term "sale of electric energy at wholesale" when used in this subchapter, means a sale of electric energy to any person for resale.

(e) "Public utility" defined

The term "public utility" when used in this subchapter and subchapter III of this chapter means any person who owns or operates facilities subject to the jurisdiction of the Commission under this subchapter (other than facilities subject to such jurisdiction solely by reason of section 824e(e), 824e(f),[1] 824i, 824j, 824j-1, 824k, 824*o*, 824p, 824q, 824r, 824s, 824t, 824u, or 824v of this title).

(f) United States, State, political subdivision of a State, or agency or instrumentality thereof exempt

No provision in this subchapter shall apply to, or be deemed to include, the United States, a State or any political subdivision of a State, an electric cooperative that receives financing under the Rural Electrification Act of 1936 (7 U.S.C. 901 *et seq.*) or that sells less than 4,000,000 megawatt hours of electricity per year, or any agency, authority, or instrumentality of any one or more of the foregoing, or any corporation which is wholly owned, directly or indirectly, by any one or more of the foregoing, or any officer, agent, or employee of any of the foregoing acting as such in the course of his official duty, unless such provision makes specific reference thereto.

(g) Books and records

(1) Upon written order of a State commission, a State commission may examine the books, accounts, memoranda, contracts, and records of—

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[1] So in original. Section 824e of this title does not contain a subsec. (f).

(A) an electric utility company subject to its regulatory authority under State law,

(B) any exempt wholesale generator selling energy at wholesale to such electric utility, and

(C) any electric utility company, or holding company thereof, which is an associate company or affiliate of an exempt wholesale generator which sells electric energy to an electric utility company referred to in subparagraph (A),

wherever located, if such examination is required for the effective discharge of the State commission's regulatory responsibilities affecting the provision of electric service.

(2) Where a State commission issues an order pursuant to paragraph (1), the State commission shall not publicly disclose trade secrets or sensitive commercial information.

(3) Any United States district court located in the State in which the State commission referred to in paragraph (1) is located shall have jurisdiction to enforce compliance with this subsection.

(4) Nothing in this section shall—

(A) preempt applicable State law concerning the provision of records and other information; or

(B) in any way limit rights to obtain records and other information under Federal law, contracts, or otherwise.

(5) As used in this subsection the terms "affiliate", "associate company", "electric utility company", "holding company", "subsidiary company", and "exempt

wholesale generator" shall have the same meaning as when used in the Public Utility Holding Company Act of 2005 [42 U.S.C. 16451 et seq.].

2. 16 U.S.C. 824d provides:

Rates and charges; schedules; suspension of new rates; automatic adjustment clauses

(a) Just and reasonable rates

All rates and charges made, demanded, or received by any public utility for or in connection with the transmission or sale of electric energy subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) Preference or advantage unlawful

No public utility shall, with respect to any transmission or sale subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Schedules

Under such rules and regulations as the Commission may prescribe, every public utility shall file with the Commission, within such time and in such form as the Commission may designate, and shall keep open in con-

venient form and place for public inspection schedules showing all rates and charges for any transmission or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Notice required for rate changes

Unless the Commission otherwise orders, no change shall be made by any public utility in any such rate, charge, classification, or service, or in any rule, regulation, or contract relating thereto, except after sixty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the sixty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Suspension of new rates; hearings; five-month period

Whenever any such new schedule is filed the Commission shall have authority, either upon complaint or upon its own initiative without complaint, at once, and, if it so orders, without answer or formal pleading by the public utility, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with

such schedules and delivering to the public utility affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of such five months, the proposed change of rate, charge, classification, or service shall go into effect at the end of such period, but in case of a proposed increased rate or charge, the Commission may by order require the interested public utility or public utilities to keep accurate account in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts are paid, and upon completion of the hearing and decision may by further order require such public utility or public utilities to refund, with interest, to the persons in whose behalf such amounts were paid, such portion of such increased rates or charges as by its decision shall be found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the public utility, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible.

(f) Review of automatic adjustment clauses and public utility practices; action by Commission; "automatic adjustment clause" defined

(1) Not later than 2 years after November 9, 1978, and not less often than every 4 years thereafter, the Commission shall make a thorough review of automatic adjustment clauses in public utility rate schedules to examine—

(A) whether or not each such clause effectively provides incentives for efficient use of resources (including economical purchase and use of fuel and electric energy), and

(B) whether any such clause reflects any costs other than costs which are—

(i) subject to periodic fluctuations and

(ii) not susceptible to precise determinations in rate cases prior to the time such costs are incurred.

Such review may take place in individual rate proceedings or in generic or other separate proceedings applicable to one or more utilities.

(2) Not less frequently than every 2 years, in rate proceedings or in generic or other separate proceedings, the Commission shall review, with respect to each public utility, practices under any automatic adjustment clauses of such utility to insure efficient use of resources (including economical purchase and use of fuel and electric energy) under such clauses.

(3) The Commission may, on its own motion or upon complaint, after an opportunity for an evidentiary hearing, order a public utility to—

(A) modify the terms and provisions of any automatic adjustment clause, or

(B) cease any practice in connection with the clause,

if such clause or practice does not result in the economical purchase and use of fuel, electric energy, or other items, the cost of which is included in any rate schedule under an automatic adjustment clause.

(4) As used in this subsection, the term "automatic adjustment clause" means a provision of a rate schedule which provides for increases or decreases (or both), without prior hearing, in rates reflecting increases or decreases (or both) in costs incurred by an electric utility. Such term does not include any rate which takes effect subject to refund and subject to a later determination of the appropriate amount of such rate.

3. 16 U.S.C. 824e provides:

Power of Commission to fix rates and charges; determination of cost of production or transmission

(a) Unjust or preferential rates, etc.; statement of reasons for changes; hearing; specification of issues

Whenever the Commission, after a hearing held upon its own motion or upon complaint, shall find that any rate, charge, or classification, demanded, observed, charged, or collected by any public utility for any transmission or sale subject to the jurisdiction of the Com-

mission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order. Any complaint or motion of the Commission to initiate a proceeding under this section shall state the change or changes to be made in the rate, charge, classification, rule, regulation, practice, or contract then in force, and the reasons for any proposed change or changes therein. If, after review of any motion or complaint and answer, the Commission shall decide to hold a hearing, it shall fix by order the time and place of such hearing and shall specify the issues to be adjudicated.

(b) Refund effective date; preferential proceedings; statement of reasons for delay; burden of proof; scope of refund order; refund orders in cases of dilatory behavior; interest

Whenever the Commission institutes a proceeding under this section, the Commission shall establish a refund effective date. In the case of a proceeding instituted on complaint, the refund effective date shall not be earlier than the date of the filing of such complaint nor later than 5 months after the filing of such complaint. In the case of a proceeding instituted by the Commission on its own motion, the refund effective date shall not be earlier than the date of the publication by the Commission of notice of its intention to initiate such proceeding nor later than 5 months after the publication date. Upon institution of a proceeding under this section, the Commission shall give to the decision of such proceeding the

same preference as provided under section 824d of this title and otherwise act as speedily as possible. If no final decision is rendered by the conclusion of the 180-day period commencing upon initiation of a proceeding pursuant to this section, the Commission shall state the reasons why it has failed to do so and shall state its best estimate as to when it reasonably expects to make such decision. In any proceeding under this section, the burden of proof to show that any rate, charge, classification, rule, regulation, practice, or contract is unjust, unreasonable, unduly discriminatory, or preferential shall be upon the Commission or the complainant. At the conclusion of any proceeding under this section, the Commission may order refunds of any amounts paid, for the period subsequent to the refund effective date through a date fifteen months after such refund effective date, in excess of those which would have been paid under the just and reasonable rate, charge, classification, rule, regulation, practice, or contract which the Commission orders to be thereafter observed and in force: *Provided,* That if the proceeding is not concluded within fifteen months after the refund effective date and if the Commission determines at the conclusion of the proceeding that the proceeding was not resolved within the fifteen-month period primarily because of dilatory behavior by the public utility, the Commission may order refunds of any or all amounts paid for the period subsequent to the refund effective date and prior to the conclusion of the proceeding. The refunds shall be made, with interest, to those persons who have paid those rates or charges which are the subject of the proceeding.

(c) Refund considerations; shifting costs; reduction in revenues; "electric utility companies" and "registered holding company" defined

Notwithstanding subsection (b) of this section, in a proceeding commenced under this section involving two or more electric utility companies of a registered holding company, refunds which might otherwise be payable under subsection (b) of this section shall not be ordered to the extent that such refunds would result from any portion of a Commission order that (1) requires a decrease in system production or transmission costs to be paid by one or more of such electric companies; and (2) is based upon a determination that the amount of such decrease should be paid through an increase in the costs to be paid by other electric utility companies of such registered holding company: *Provided,* That refunds, in whole or in part, may be ordered by the Commission if it determines that the registered holding company would not experience any reduction in revenues which results from an inability of an electric utility company of the holding company to recover such increase in costs for the period between the refund effective date and the effective date of the Commission's order. For purposes of this subsection, the terms "electric utility companies" and "registered holding company" shall have the same meanings as provided in the Public Utility Holding Company Act of 1935, as amended.[1]

(d) Investigation of costs

The Commission upon its own motion, or upon the request of any State commission whenever it can do so without prejudice to the efficient and proper conduct of

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[1] See References in Text note below.

its affairs, may investigate and determine the cost of the production or transmission of electric energy by means of facilities under the jurisdiction of the Commission in cases where the Commission has no authority to establish a rate governing the sale of such energy.

(e) Short-term sales

(1) In this subsection:

(A) The term "short-term sale" means an agreement for the sale of electric energy at wholesale in interstate commerce that is for a period of 31 days or less (excluding monthly contracts subject to automatic renewal).

(B) The term "applicable Commission rule" means a Commission rule applicable to sales at wholesale by public utilities that the Commission determines after notice and comment should also be applicable to entities subject to this subsection.

(2) If an entity described in section 824(f) of this title voluntarily makes a short-term sale of electric energy through an organized market in which the rates for the sale are established by Commission-approved tariff (rather than by contract) and the sale violates the terms of the tariff or applicable Commission rules in effect at the time of the sale, the entity shall be subject to the refund authority of the Commission under this section with respect to the violation.

(3) This section shall not apply to—

(A) any entity that sells in total (including affiliates of the entity) less than 8,000,000 megawatt hours of electricity per year; or

(B) an electric cooperative.

(4)(A) The Commission shall have refund authority under paragraph (2) with respect to a voluntary short term sale of electric energy by the Bonneville Power Administration only if the sale is at an unjust and unreasonable rate.

(B) The Commission may order a refund under subparagraph (A) only for short-term sales made by the Bonneville Power Administration at rates that are higher than the highest just and reasonable rate charged by any other entity for a short-term sale of electric energy in the same geographic market for the same, or most nearly comparable, period as the sale by the Bonneville Power Administration.

(C) In the case of any Federal power marketing agency or the Tennessee Valley Authority, the Commission shall not assert or exercise any regulatory authority or power under paragraph (2) other than the ordering of refunds to achieve a just and reasonable rate.

RESPONDENT'S BRIEF

(13)

No. 08-674

Supreme Court, U.S.
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In The

Supreme Court of the United States

NRG POWER MARKETING, LLC, ET AL.,

Petitioners,

v.

MAINE PUBLIC UTILITIES COMMISSION, ET AL.,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The District Of Columbia Circuit

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QUESTION PRESENTED

Section 206 of the Federal Power Act ("FPA"), 16 U.S.C. § 824e(a), requires that all rates for the transmission and sale of electricity in interstate commerce be "just and reasonable." Under the *Mobile-Sierra* doctrine, when sellers and purchasers enter into freely negotiated wholesale energy contracts, the Federal Energy Regulatory Commission ("FERC" or "Commission") must presume that the negotiated rate is just and reasonable, and parties to the contract may overcome that presumption and avoid their contractual bargain only by showing that the contract rate seriously harms the "public interest." In this case, the Respondents were parties to a contested FERC proceeding but objected to a settlement agreement agreed to by other parties and approved by FERC. The contested settlement purported to apply the restrictive *Mobile-Sierra* presumption to challenges by both settling and non-settling parties to rates that will be determined in the future. That is, the settling parties sought by contract to restrict non-contracting parties' statutory right to challenge rates as unjust or unreasonable.

The question presented is:

Whether the Commission may approve a contested settlement agreement where the settling parties propose to deprive non-contracting participants of their statutory rights to challenge tariff rates as being unjust and unreasonable except under the much more stringent and "practically insurmountable" public interest mode of review.

CORPORATE DISCLOSURE STATEMENT

Richard Blumenthal, Attorney General for the State of Connecticut, hereby submits that the Office of the Attorney General is a governmental party exempt from any reporting requirement under Rule 29.6. The CTAG is the chief civil legal officer of the State of Connecticut and has no parent corporation or publicly held stock.

The Maine Public Utilities Commission hereby submits that it is a governmental party exempt from any reporting requirement under Rule 29.6. MPUC has no parent corporation or publicly held stock.

Martha Coakley, Attorney General for the Commonwealth of Massachusetts, hereby submits that the Office of the Attorney General is a governmental party exempt from any reporting requirement under Rule 29.6. The MassAG is the chief civil legal officer of the Commonwealth of Massachusetts and has no parent corporation or publicly held stock.

The Industrial Energy Consumer Group is a non-profit trade association incorporated under the laws of the state of Maine. The IECG has no parent company or affiliated companies. The IECG was created and exists to advance the interests of industrial users of electricity in Maine and other interested persons. There are no ownership interests associated with the IECG.

CORPORATE DISCLOSURE STATEMENT – Continued

NEPOOL Industrial Customer Coalition is a continuing ad hoc association of large industrial and commercial end-users of electricity in New England operated for the purposes of representing the interests of industrial energy consumers before regulatory and legislative bodies. NICC does not issue securities to the public and is not owned by any publicly held company.

NSTAR Electric & Gas Corporation ("NSTAR") is a wholly-owned subsidiary of NSTAR, a public utility holding company which has issued securities to the public. In addition, NSTAR Electric & Gas Corporation's affiliate, NSTAR Electric Company, has issued preferred stock and debt securities to the public. No other affiliates of NSTAR Electric & Gas Corporation have outstanding securities to the public.

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STATEMENT

Over the objection of the Respondents, FERC approved a settlement agreement that "redesigned New England's capacity market" for electricity. Pet. App. 1a. Among the terms of the settlement are a mechanism for establishing the future price of wholesale energy capacity through auctions and a set of fixed prices for wholesale energy capacity for a three-year transition period. Despite the Respondents' objection, FERC approved the settlement, its auction mechanism, the resulting rates, and the transition rates that now define the terms of service for all wholesale customers in New England, including the Respondents. FERC may, of course, establish the terms and conditions for service to the Respondents, but only if it determines the rates are just and reasonable. The issue presented in this case is what form of just and reasonable review applies to a challenge by the Respondents to auction and transition rates that the settlement directly imposes upon them.

Critically, therefore, this case does not present the issue raised and argued by the Petitioners. The Petitioners act as though the rates in question were established by a run-of-the-mill bilateral wholesale energy contract and are being challenged by entities "indirectly affected by a contract rate," such as "consumer[s]" who are members of the general public. Pet. Br. 3; *see also* Pet Br. 18, 24, 28, 29, 37, 41. The Petitioners then argue that excepting such challenges from the *Mobile-Sierra* doctrine would "see

the [doctrine] overwhelmed by hordes of motivated non-parties lying in wait not far behind," making the Court's *Mobile-Sierra* doctrine "an exercise in futility" that "provides no stability at all." Pet. Br. 18. In fact, the Respondents are not indirectly affected members of the general public, but rather active participants in both the relevant wholesale market *and* parties to the contested FERC proceeding that resulted in approval of these rates. Indeed, Respondent NSTAR purchases 25 percent of New England's capacity obligations. The settlement, however, purports to bind NSTAR to pay certain rates for that capacity. Thus, whether *Mobile-Sierra* public-interest review applies to a challenge by an indirectly affected member of the general public is an interesting question, but it is not one that is before this Court in this case.

When the status and interests of the parties are properly framed, it is apparent that the *Mobile-Sierra* presumption of reasonableness does not apply for two reasons. First, as FERC acknowledges, Br. 28-32, the rates produced by the settlement are not "contract" rates to which the *Mobile-Sierra* doctrine could apply in the first place. Second, even if those rates were treated like genuine contract rates, the *Mobile-Sierra* doctrine does not apply to challenges by a third party that, against its will, is subjected to rates agreed upon by others. The Petitioners are certainly free to agree to energy rates among themselves, and agree that they may not back out of that agreement if they later find it disadvantageous. But there is no basis in

statute, precedent, or logic for presuming that the rates to which they agreed are just and reasonable as applied to a third party whom they seek to bind to their bargain over its express objection. That directly affected third party is entitled to have FERC assess its challenge to the rates under the traditional just and reasonable standard of review. The decision of the Court of Appeals should be affirmed.

I. STATUTORY BACKGROUND

Under Section 205 of the Federal Power Act ("FPA"), all rates filed with FERC must be "just and reasonable." 16 U.S.C. § 824d. Section 206 provides that "upon complaint" FERC must determine whether a challenged rate is "unjust, unreasonable, unduly discriminatory or preferential." 16 U.S.C. § 824e.

In *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332 (1956) ("*Mobile*") and *Federal Power Comm'n v. Sierra Pacific Power Co.*, 350 U.S. 348, 355 (1956) ("*Sierra*"), the Court recognized that buyers and sellers that have agreed to fix rates by contract do not have the right to seek to modify those rates by regulatory interdiction simply because it is in their private interest to do so.

Under the *Mobile-Sierra* doctrine, when sellers enter into freely negotiated wholesale energy contracts with purchasers, the Commission must presume that, as between the parties, the negotiated rate is "just and reasonable." *See Morgan Stanley*

Capital Group, Inc. v. Pub. Util. Dist. No. 1, 128 S.Ct. 2733, 2737 (2008); *see also* 16 U.S.C. §§ 824d, 824e. In wholesale markets, the buyer and seller are often "sophisticated businesses enjoying presumptively equal bargaining power, who could be expected to negotiate a 'just and reasonable' rate as between the two of them." *Verizon Communications v. FCC*, 535 U.S. 467, 479 (2002).

The Commission and the Courts of Appeals have referred to the much more restrictive mode of review applicable under the *Mobile-Sierra* doctrine to rate challenges by contracting parties as the "public interest standard," as opposed to the statutory "just and reasonable standard." *Morgan Stanley*, 128 S.Ct. at 2740 (citing *Southern Co. Servs., Inc., et al.*, 39 FERC ¶ 63,026 at 65,134, 65,141 (1987); *Kansas Cities v. FERC*, 723 F.2d 82, 87-88 (D.C. Cir. 1983); *Northeast Utils. Serv. Co. v. FERC*, 993 F.2d 937, 961 (1st Cir. 1993)). As this Court has observed, however, this "nomenclature" refers to the differing application of the just and reasonable standard to contract rates. *Id.* (citing *Philadelphia Elec. Co.*, 58 F.P.C. 88, 90 (1977)).

Courts of Appeals have characterized the *Mobile-Sierra* public interest standard as being "much more restrictive than the FPA's 'just and reasonable' standard, even describing the burden of the public interest standard as 'practically insurmountable' and 'almost insurmountable.'" *Potomac Elec. Power Co. v. FERC*, 210 F.3d 403, 407-408 (D.C. Cir. 2000) (citations omitted).

Although the public interest showing is the default mode of review of contract modifications sought by a contracting party, this Court has held that parties to a contract can agree that the *Mobile-Sierra* presumption shall not apply. *See United Gas Pipe Line Co. v. Memphis Light, Gas & Water Div.*, 358 U.S. 103, 110-113 (1958) ("*Memphis*"). "[I]n the absence of any contractual relationship rates determined ex parte by the seller may be filed under § 4(d) [of the Natural Gas Act]. . . . We perceive no tenable basis of distinction between the filing of such a rate in the absence of contract and a similar filing under an agreement which explicitly permits it." *Id.* at 112-113 (internal citations omitted). Thus, contracting parties can agree that they may challenge the contract rate if it results in an unfair rate of return, not just if it violates the public interest. *See Morgan Stanley*, 128 S.Ct. at 2739 (citing *Papago Tribal Util. Auth. v. FERC*, 723 F.2d 950, 953, 955 (D.C. Cir. 1983); *Louisiana Power & Light Co. v. FERC*, 587 F.2d 671, 675-676 (5th Cir. 1979)). Such provisions are commonly referred to as "*Memphis* clauses."

II. THE CONTESTED SETTLEMENT

This case arose from a highly contested FERC proceeding in which ISO New England, Inc. ("ISO New England"), the independent system operator that manages the reliability of the bulk power system in New England, filed changes to its market rules tariff to address deficiencies in the mechanism for

procuring generation capacity. Pet. App. 105a. After two years of litigation, 107 parties reached a settlement, while eight parties, including the Respondents here, opposed the settlement. *Id.* at 110a. Thus, there was no agreement between the settling parties and the Respondents. That settlement was subject to approval by the Commission.

The proposed settlement created a forward capacity market ("FCM"), in which an annual auction mechanism would determine the single rate paid to electric capacity resources three years in advance of when that capacity would be needed. *Id.* The auctions would procure the generating capacity required to satisfy the installed capacity requirement, which is the minimum level of capacity that ISO New England determines is necessary to maintain the reliability of the grid. *Id.* at 112a. ISO New England would then directly allocate the cost of such capacity to each utility serving end-use customers based on its proportional share of peak load. *Id.* The FCM would include an auction-based mechanism for setting a tariff-based regional clearing price that would apply to all New England market participants. *Id.* at 118a.

Because there would be a three-year gap between the first auction and the year that the capacity procured through the auction would be provided, the settling parties agreed that all qualifying capacity resources would receive payments according to a schedule of rates during a transition period between December 1, 2006 and ending on June 1, 2010, whether or not they were needed for reliability. *Id.* at

116a. The cost of these payments similarly would be allocated to utilities based on their proportionate share of peak load. *Id.* at 117a.

The settlement agreement contains a provision (§ 4.C) purporting to impose the *Mobile-Sierra* presumption against all challenges to the capacity clearing prices derived from the annual forward capacity auctions ("FCA") and challenges to the transition period payments, regardless of whether the challenge is made "by a Settling Party, a non-Settling Party, or the FERC acting *sua sponte*." *Id.* at 193a-194a (quoting § 4.C of the settlement agreement). The settlement agreement also contains a *Memphis* clause exempting all other terms of the settlement agreement from the operation of the *Mobile-Sierra* presumption. *Id.* at 194a.

FERC approved the *Mobile-Sierra* provision, noting that it has permitted the use of similar provisions in the past, citing a string of cases dating back to 2003. *Id.* at 200a-201a. Finding that it retained authority to protect non-settling parties under the public interest standard of review, FERC found the provision "reasonable." It also based its finding of reasonableness on a provision in the settlement agreement that permits parties to challenge ISO New England's "informational filings" on the auction results under the just and reasonable mode of review when ISO New England files them under Section 205. *Id.* at 78a, 201a-202a. Finally, FERC concluded that it was appropriate to apply the

Mobile-Sierra presumption to non-settling parties in order to achieve "contractual stability." *Id.* at 202a.

Because the fixed-rate transition payments and auction based mechanism produce tariff based rates of general applicability to all New England market participants, the contested settlement directly binds the Respondents to accept the rates and conditions of service resulting from transition payments and the auction in precisely the same manner as the contested settlement agreement binds all of the market participants that agreed to the settlement. As noted above, NSTAR is directly responsible for 25 percent of New England's load. NSTAR therefore is subject to the transition rates and the rates that result from the auction although it objected to the settlement.

III. THE DECISION BELOW

In the decision below, the Court of Appeals held that, in approving the settlement agreement, the Commission unlawfully deprived non-settling parties—including the Respondents—"of their statutory right" under the Federal Power Act "to challenge rates under the 'just and reasonable' standard." *Id.* at 19a. The court found that "[t]his case is clearly outside the scope of the *Mobile-Sierra* doctrine." *Id.* at 22a. The court stated that *Mobile-Sierra* is invoked when "one party to a rate contract on file with FERC attempts to effect a unilateral rate change by asking FERC to relieve its

obligations under a contract whose terms are no longer favorable to that party." *Id.* (quoting *Maine PUC v. FERC*, 454 F.3d 278, 284 (D.C. Cir. 2006)). The court found that "the settling parties are attempting to thrust the 'public interest' standard of review upon non-settling third parties who have vociferously objected to the terms of the settlement agreement." *Id.* The court noted that "[i]t goes without saying that a contract cannot bind a nonparty." *Id.* (quoting *EEOC v. Waffle House, Inc.*, 534 U.S. 279 (2002)). The court stated that the purpose of the *Mobile-Sierra* doctrine is to "preserve the terms of the bargain as between the contracting parties." *Id.* (citing *Atlantic City Elec. Co. v. FERC*, 295 F.3d 1, 14 (D.C. Cir. 2002)). Accordingly "when a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply; the proper standard of review remains the 'just and reasonable' standard in section 206 of the Federal Power Act." *Id.*

The court rejected FERC's justifications for approving the *Mobile-Sierra* provision—that the public interest showing will only apply to future challenges to a narrow category of rates or that non-settling parties are adequately safeguarded under the Commission's retained authority under *Mobile-Sierra*—holding that approval of the agreement still deprives non-settling parties of their statutory right to have rate challenges adjudicated under the ordinary "just and reasonable" showing. *Id.* at 22a-23a. The court also rejected FERC's argument

that the Commission has routinely approved contracts that apply the public interest review to non-contracting parties, noting that the Commission has only done so since 2002 and that none of the decisions to which FERC cited has been subject to judicial review on the *Mobile-Sierra* issue. *Id.* at 23a.

Finally, with respect to the need for contract stability, the court explained that "the *Mobile-Sierra* doctrine is designed to ensure contract stability *as between the contracting parties—i.e.*, to make it more difficult for either party to shirk its contractual obligations." *Id.* at 24a (citing *Atlantic City*, 295 F.3d at 14) (emphasis in original). The court observed that "[i]t makes no sense to say that the values of 'stability' and 'certainty' are furthered by applying the deferential standard of review to the eight parties that *refused* to agree to the terms of the settlement." *Id.* (emphasis in original).

SUMMARY OF ARGUMENT

The *Mobile-Sierra* doctrine provides that freely negotiated contracts by sophisticated buyers and sellers are presumed "'just and reasonable' as between the two of them." *Morgan Stanley*, 128 S.Ct. at 2746 (citations omitted). When a party to such a contract challenges it, FERC may only provide relief if the party shows that the public interest, strictly defined, will be injured by the contract. The Petitioners seek to impose that "public interest"

standard upon the Respondents, thereby drastically limiting the Respondents' ability to challenge rates imposed under a settlement that the Petitioners adopted, but to which the Respondents objected. Applying the *Mobile-Sierra* doctrine in that manner would unmoor it from its foundations, converting it to a sword by which contracting parties can bind third parties to rates to which they never agreed.

I. As an initial matter, the rates produced by the settlement are not "contract rates" to which the *Mobile-Sierra* presumption could apply in the first place. The rates at issue in this proceeding are fundamentally different from the typical bilateral contracts that were at issue in *Mobile*, *Sierra*, and *Morgan Stanley*. The transition payments and the FCA auction results are tariff rates of general applicability throughout New England. The *Mobile-Sierra* public interest standard applies only to rates arising from freely negotiated private contracts, and not to tariff rates or to rates established as a result of a regulatory process. FERC agrees that "neither of the two types of rates to which Section 4.C of the settlement applies . . . is subject to the statutory *Mobile-Sierra* presumption, and the Commission was not *required* to apply the public interest standard to its review of those rates." FERC Br. 30. FERC's concession is a sound one that this Court should accept.

II. Even assuming the *Mobile-Sierra* doctrine could apply to general tariffs, its presumption of reasonableness does not apply to challenges brought

by entities that objected to the settlement that produced the rates. The premise of the doctrine is that the sophisticated parties that enter wholesale energy contracts should be bound by their bargain, for they can "be expected to negotiate a 'just and reasonable' rate as between the two of them." The doctrine therefore restricts the ability of a contracting party to obtain regulatory relief from the obligations it voluntarily incurred. But the doctrine has no application to efforts by contracting parties to bind third parties to the contractual terms. The FPA properly holds a contracting party to an "improvident bargain"; but the statute cannot reasonably be construed as binding a non-settling party to an "improvident bargain" to which it objected, but which was thrust upon it. The non-settling party is entitled to have FERC review the rates under the ordinary just and reasonable standard.

The Petitioners counter that allowing non-parties to challenge contractual rates under the ordinary standard would eviscerate the *Mobile-Sierra* doctrine because "hordes" of consumers indirectly affected by the rates would be able to file challenges. But the Respondents are not "indirectly affected" parties. To the contrary, the settlement created a tariff mechanism that sets the terms and conditions of service for all market participants in New England, including the Respondents. The *Mobile-Sierra* doctrine does not permit settling parties to contractually bind non-settling third parties to limit their challenges to a tariff derived from the

settlement rate mechanism simply because the parties have agreed among themselves that such challenges should be limited. As the Court of Appeals observed, the Petitioners' position conflicts with the fundamental principle of contract law that a contract cannot bind a non-party.

The Petitioners' various other attacks on the Court of Appeals' decision are unfounded. Although the Court of Appeals used the common nomenclature for the *Mobile-Sierra* doctrine that this Court clarified in *Morgan Stanley*, its reasoning did not depend on its use of that nomenclature. And the Court of Appeals' ruling does not conflict with any lower court precedent or with prior FERC practice. Indeed, it is the Petitioners' position that conflicts with this Court's longstanding recognition that the FPA does not presume that market-based rates are inherently just and reasonable.

III. Because the *Mobile-Sierra* doctrine does not apply to challenges by the Respondents to rates produced by the settlement, the Court of Appeals' judgment should be affirmed. FERC argues, however, that it has the authority to impose a *Mobile-Sierra* public interest presumption in the absence of any contract from which such presumption might arise. As an initial matter, FERC did not expressly raise this argument below and did not assert it in its brief in opposition. The Court should therefore affirm the Court of Appeals' judgment without reaching this argument. FERC is also wrong on the merits. FERC contends that it has the discretion to apply a public

interest standard to challenges by the Respondents under its broad authority to approve contested settlement agreements that it believes will produce just and reasonable rates. FERC Br. 32. But neither the FPA nor any court precedent supports the proposition that FERC may simply rewrite the terms of the FPA based upon what FERC believes may produce just and reasonable rates. While FERC has the authority to establish or approve a mechanism to set capacity costs, it does not have the discretion to abrogate the Respondents' statutory rights under Section 206. FERC is not permitted to use its discretion to determine that the public interest standard may be applied outside a contract context.

IV. Finally, the Petitioners are wrong in asserting that affirmance would threaten industry stability. The narrow issue before the Court is whether an entity that objected to a settlement can challenge rates produced by the settlement and imposed on them under the ordinary just and reasonable standard. A positive answer to the question will not undermine the *Mobile-Sierra* doctrine and the stability the doctrine advances. Settling parties reasonably expect challenges by objectors. More generally, parties that enter contracts understand that they generally cannot bind third parties to the contractual terms. FERC has applied the *Mobile-Sierra* public interest standard to non-parties only since 2002, yet there is no evidence that industry stability was threatened before then. Proving that rates are unjust and unreasonable is a

challenge even absent the *Mobile-Sierra* presumption; its application to situations like the present one poses no threat to the industry.

ARGUMENT

I. NEITHER THE SETTLEMENT AGREEMENT NOR THE RATES GENERATED UNDER THE AGREEMENT FALL WITHIN THE *MOBILE-SIERRA* DOCTRINE

The FPA provides for two rate setting mechanisms. Rates may be set bilaterally by contract or unilaterally by tariff. *Mobile*, 350 U.S. at 343 (parties may establish a tariff rate "*ex parte*, and change at will, the rates offered to prospective customers; or to fix by contract, and change only by mutual agreement, the rate agreed upon with a particular customer . . . ").

The *Mobile-Sierra* public interest standard applies only to rates arising from freely negotiated private contracts. FERC agrees that the auction results, "although possessing certain characteristics of contracts, do not constitute contracts between buyers and sellers," FERC Br. 30, that would "require the Commission to apply the public interest standard." FERC Br. 31. Similarly with respect to the non-settling parties, "the transition payments do not resemble contractually negotiated rates at all." *Id.* In short, FERC itself does not attempt to justify its imposition of the *Mobile-Sierra* presumption on any

Mobile-Sierra or contract theory. FERC is correct that the *Mobile-Sierra* doctrine does not apply to the settlement terms at issue because they do not constitute freely negotiated contracts.[1]

A. The Forward Capacity Auction Results Are Not Contract Rates Subject To The *Mobile-Sierra* Doctrine

The contested settlement agreement is a negotiated contract between the settling parties. However, the tariffs that set the transition payments

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[1] Although the Court of Appeals did not rule on this issue, the Respondents have preserved it (*see* Resp. BIO 10-12) and its resolution is "essential to the analysis of the decisions below or to the correct disposition of the other issues," and therefore is "fairly comprised by the question presented." *City of Sherrill* v. *Oneida Indian Nation of N.Y.*, 544 U.S. 197, 214 n.8 (2005) (quoting R. Stern, E. Gressman, S. Shapiro, & K. Geller, *Supreme Court Practice* 414 (8th ed. 2002)); *see also Ballard* v. *Commissioner*, 544 U.S. 40, 46-47 & n.2 (2005) (addressing "a question anterior" to the "questions the parties raised"). This case is an appeal of FERC's approval of Section 4.C of the proposed settlement, which provides that any future challenge to auction results or transition payments would be reviewed under the public-interest standard. Yet FERC now disclaims having approved that provision based on the *Mobile-Sierra* doctrine, and asserts that the doctrine does not apply to this case. FERC Br. 22-23. To ignore that concession, assume that this case involves a contract to which *Mobile-Sierra* applies, and then resolve whether the doctrine applies to challenges by directly affected third parties would be tantamount to issuing an advisory opinion. The Court should either dismiss the petition as improvidently granted or address the threshold question whether the *Mobile-Sierra* doctrine applies to this case.

and the rules for conducting auctions are by definition not contract rates. Those tariff provisions provide a mechanism—auctions—for setting rates that will become the terms of service to both contracting and non-contracting parties. Those rates are clearly distinct from the rates established by contract and applicable only to the contracting parties. The FCA auction differs fundamentally from bilateral contracts. The settlement provisions for transition period payments and for payments under the forward capacity market were to be implemented through then yet-to-be-developed tariff revisions. *Order Accepting Proposed Settlement Agreement*, Pet. App. 118a. These tariff revisions are rules of general applicability.

The settlement agreement that the Petitioners seek to impose upon non-contracting third parties is fundamentally different from the privately negotiated bilateral energy contracts that were at issue in *Morgan Stanley*. Instead, the settlement agreement "emanated from a highly contested adjudicatory proceeding before the Commission and involves a broad, public matter." Pet. App. 228a (quoting FERC commissioners Kelly and Wellinghoff); *cf. Morgan Stanley*, 128 S.Ct. at 2746. Whereas the *Mobile-Sierra* doctrine assumes that "sophisticated businesses enjoying presumptively equal bargaining power . . . could be expected to negotiate a 'just and reasonable' rate as between the two of them," *Verizon*, 535 U.S. at 479, "no 'commonsense notion' would hold that the

115 *parties* to the adjudication of this matter enjoy presumptively equal bargaining power." *Id.*[2]

The Petitioners and amici repeatedly mischaracterize the results from the FCM auction as "contracts" rather than "tariffs." Pet. Br. 35, 46-52; EPSA Br. 22-23. They argue that auction rates become contract rates because the auction result constitutes an "offer" that the buyer may "accept." Pet. Br. 47; EPSA Br. 23. The Court should reject their novel attempt to transform tariff rates into contract rates. A generally applicable rate is a tariff rate regardless of whether the consumer chooses to accept service under the tariff rate. The Petitioners' claim that a tariff rate becomes a contract rate once a load serving entity agrees to take service under the tariff rate would subsume all tariff rates under the *Mobile-Sierra* doctrine. Such a construction would eviscerate the distinction between tariff rates and contract rates and would be directly contrary to this Court's lengthy analysis in *Morgan Stanley*, 128 S.Ct. at 2740, 2746 n.3, 2749 n.6.

FERC acknowledges that the auction results and the rates thereby generated are not contract rates but are tariff rates. FERC states that the auction results "although possessing certain characteristics of contracts, do not constitute contracts between buyers and sellers," FERC Br. 30, which would "require the

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[2] This is why settlements are not presumed to be just and reasonable. *Mobil Oil Corp. v. FPC*, 417 U.S. 283, 314 (1974).

Commission to apply the public interest standard." FERC Br. 31. Because the FCM auction results are plainly tariff rates, no *Mobile-Sierra* presumption can apply.

B. The Transition Payments Are Not Contract Rates Subject To The *Mobile-Sierra* Doctrine

The transition payments are similarly not a product of a contract freely negotiated outside of the regulatory process and subject to *Mobile-Sierra*. As FERC states, "[a]lthough the settlement represented an agreement among the signators, it was not a private contract of the sort at issue in *Mobile*, *Sierra*, and *Morgan Stanley*. It was, rather, the resolution of a disputed proceeding before the Commission. . . ." FERC Br. 31. In addition, "[t]he transition payments apply to all suppliers and purchasers of capacity—including the contesting parties and all future entrants into the market—not just to the settling parties. As to these other participants, the transition payments do not resemble contractually negotiated rates at all." *Id.* This conclusion and the logic underlying it are unassailable.

II. THE *MOBILE-SIERRA* DOCTRINE DOES NOT APPLY TO CHALLENGES BY NON-SIGNATORIES TO A SETTLEMENT AGREEMENT

Even assuming the *Mobile-Sierra* presumption applies to the tariff rates at issue here, the

presumption would not apply to challenges asserted by the Respondents, who are non-contracting third parties directly subjected to the settlement rates. The Petitioners devote most of their energies to explaining the problems with excepting from *Mobile-Sierra* public interest review those challenges brought by members of the general public who are indirectly affected by wholesale energy contracts. That situation, however, is not before the Court. The settlement purports to bind the Respondents—including NSTAR, which purchases 25 percent of New England's capacity obligations—to pay certain rates for that capacity. While the *Mobile-Sierra* doctrine sensibly presumes that contractual rates are just and reasonable as between the contracting parties, there is no basis upon which to presume that contractual rates are just and reasonable when imposed upon non-parties. The Respondents should be entitled to challenge rates established under the settlement under the ordinary just and reasonable standard.

A. A Prerequisite To The Application Of The *Mobile-Sierra* Doctrine Is A Willing Buyer And A Willing Seller

In *Mobile* and *Sierra*, the Court recognized that buyers and sellers that have agreed to fix rates by contract do not have the right to seek to modify those rates by regulatory interdiction simply because it is in their private interest to do so. In *Mobile*, the Court held that a supplier under a contract does not have the right to change its rate contracts unilaterally by

filing a new tariff schedule and that such a filing is a "nullity." 350 U.S. at 336. In *Sierra*, the Court held that a selling party asking a regulatory authority to modify a contract rate must demonstrate that the existing rate is "so low as to adversely affect the public interest—as where it might impair the financial ability of the public utility to continue its service, cast upon other consumers an excessive burden, or be unduly discriminatory." 350 U.S. at 355.

The Court explained that:

> [W]hile it may be that the Commission may not normally impose upon a public utility a rate which would produce less than a fair return, it does not follow that the public utility may not itself agree by contract to a rate affording less than a fair return or that, if it does so, it is entitled to be relieved of its improvident bargain.

Id. The Court further concluded that "it is clear that a contract may not be said to be either 'unjust' or 'unreasonable' simply because it is unprofitable to the public utility." *Id.*

In *Verizon Communications Inc. v. FCC*, 535 U.S. 467 (2002), this Court emphasized that the fundamental principle underlining the application of the *Mobile-Sierra* doctrine was to hold contracting parties to their contract obligations. The Court stated:

> [i]n wholesale markets, the party charging the rate and the party charged were

> often sophisticated businesses enjoying presumptively equal bargaining power, who could be expected to negotiate a "just and reasonable" rate *as between the two of them*. . . . When commercial parties did avail themselves of rate agreements, *the principal regulatory responsibility was not to relieve a contracting party of an unreasonable rate*, *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348, 355 (1956).

Id. at 479 (emphasis added).

Thus, the *Mobile-Sierra* doctrine restricts the ability of a contracting party to seek regulatory relief from the obligations to which it agreed in the contract. In this sense, the *Mobile-Sierra* doctrine "subordinate[s] the statutory filing mechanism [of the FPA] to the broad and familiar dictates of contract law." *Borough of Lansdale v. FPC*, 494 F.2d 1104, 1113 (D.C. Cir. 1974).

B. Section 4(C) Of The Settlement Agreement Impermissibly Requires Non-Parties To A Settlement Agreement To Give Up A Statutory Right They Did Not Agree To Relinquish

Mobile-Sierra addresses the relationship between parties to a contract, and only then acts to limit those contracting parties' ability to modify unilaterally the terms of their contracts by establishing a presumption that the rates to which a willing buyer and willing seller agree are just and reasonable "as

between the two of them." *Verizon*, 535 U.S. at 479. Here, as the Court of Appeals properly held, the Respondents did not *agree* to give up a right to challenge the transition payments or the rate resulting from the auction process and that, therefore, settling parties could not require non-settling parties to relinquish rights granted under the FPA. While the Petitioners insist that the Court's decision in *Morgan Stanley* expands the *Mobile-Sierra* presumption to apply to non-settling parties, the facts and holding of *Morgan Stanley* do not support this claim.

In *Morgan Stanley*, the buyers that sought to modify contract rates after "buyer's remorse set in" were parties to the contract that they wished to alter. As the Court noted, "the contract rates between the parties included rates that were very high by historical standards," but were "substantially lower" than the rates the buyers would have paid on the spot market when they entered into the contract. In holding that the presumption of reasonableness applies to *both buying and selling parties to a contract*, the Court confirmed that the underpinning of the *Mobile-Sierra* doctrine is that "under the FPA "'[w]hen commercial parties . . . avail themselves of rate agreements, the principal regulatory responsibility [is] not to relieve a contracting party of an unreasonable rate.'" *Morgan Stanley* (quoting *Verizon*, 535 U.S. at 479).

Thus, if a party to the settlement agreement at issue in the present case challenged the transition

payments as unjust and unreasonable due to changed circumstances, *Morgan Stanley* would require FERC to apply a presumption that the rate was reasonable *as to the party that agreed to it*. *Morgan Stanley* does not, however, require or even permit FERC to apply the *Mobile-Sierra* presumption to a non-party because the prerequisite of a willing buyer and willing seller simply does not exist. To do so would hold a non-settling party to an "improvident bargain" that the non-settling party objected to in the first place.

Thus, it is no way anomalous for FERC to assess the settlement-produced rates by the public-interest standard when they are challenged by the parties to the settlement, and by the ordinary just and reasonable standard when they are challenged by the Respondents. The Petitioners assert that, "[a]s a matter of logic, the presumption of reasonableness" cannot depend on the party who is challenging the contract. Pet. Br. 35. Not so. The parties to the agreement are entitled to decide—as between themselves—what is a reasonable rate. There is every reason for FERC to presume the rate is just and reasonable as between the parties who negotiated it, but no reason for such a presumption when the rate is imposed upon a third party that did not sign the contract.

The ability of parties to contract out of the default *Mobile-Sierra* presumption through a *Memphis* clause further undermines the Petitioners' claim that FERC cannot have multiple thresholds

for reviewing a challenged rate depending upon the entity challenging the rate. Parties to a contract may agree, via a *Memphis* clause, that one party to the contract may opt out of the application of the *Mobile-Sierra* presumption—meaning the presumption would apply depending on the party that brings the challenge. Moreover, it would be absurd to construe the FPA as allowing the contracting parties to agree amongst themselves to opt out of the application of *Mobile-Sierra* via a *Memphis* clause, yet allow them to bind non-settling parties to *Mobile-Sierra* public interest review of the rates.

C. The Respondents Are Not "Indirectly Affected" Third Parties Already Protected Under The *Mobile-Sierra* Public Interest Standard

The Petitioners argue that the Court of Appeals' approach in this case creates legions of "indirectly affected" parties, such as end use consumers, who may now challenge rates. Pet. Br. 41. This would make the *Mobile-Sierra* doctrine "an exercise in futility," Pet. Br. 18, and for no good reason—the public-interest standard "exists for the precise purpose of protecting the 'public.'" Pet. Br. 27. That argument might have some force if this case involved a rate challenge brought by one of the "hordes," Pet. Br. 18, of consumers who is indirectly affected by the settlement rates. The argument has no force, however, with respect to the challenge actually before this Court.

The Respondents are not indirectly affected by the rates in question. They were parties to the underlying litigation that resulted in the settling parties' auction process and transition payments, pricing mechanisms that would apply generally to all capacity in New England. The Respondents vigorously opposed the settlement agreement between the Petitioners and the other parties. Nonetheless, in the wake of FERC's approval of the settlement, the auction process and transition payment schedule will result in tariff rates that are applicable throughout New England. The Petitioners and the settling parties have therefore created a rate scheme that directly affects not only themselves, but also sets the default tariff rate for every market participant in New England, including the non-settling Respondents.

The rates at issue, therefore, are not "inputs" that "affect" rates charged to the Respondents—they *are* the rates charged to the Respondents for wholesale service. The public interest standard does *not* "exist[ ] for the precise purpose of protecting" entities in the Respondents' position. And there are not "hordes" of third parties in the Respondents' position, such that affirming the D.C. Circuit would create a vast loophole to the *Mobile-Sierra* doctrine.

For this reason, the Court of Appeals correctly concluded that principles of contract law militate against application of the *Mobile-Sierra* doctrine to the Respondents. As the court observed, "[i]t goes without saying that a contract cannot bind a

nonparty." Pet. App. 22a (quoting *EEOC v. Waffle House, Inc.*, 534 U.S. 279, 294 (2002)). Yet applying the *Mobile-Sierra* presumption of reasonableness to a rate challenge by the Respondents would effectively bind them to a contract to which they were a non-party.

The Petitioners counter that a contract "does not 'bind' a non-party merely because its existence somehow *affects* that nonparty." Pet. Br. 41. That is correct, but no one contends otherwise. The contract here does not "merely affect" the Respondents—it purports to revoke a standard of review guaranteed to them by statute and impose on them a much more rigorous standard. Moreover, as explained above, the Respondents are not merely members of the general public who are indirectly affected by a wholesale contract rate. They are significant participants in the relevant wholesale power market and parties that objected to the settlement agreement. For this reason, *Local No. 93 Int'l Ass'n of Firefighters v. City of Cleveland*, 478 U.S. 501 (1986), upon which the Petitioners rely (Pet. Br. 42), is inapposite. The Court held in *Firefighters* that a nonsettling party's agreement was not required before a district court could approve the consent decree because the consent decree *would not affect the nonsettling party's rights*. 478 U.S. at 529-30. That is not the case here.

D. The Court Of Appeals' Approach Is Fully Consistent With Precedent

Both the Petitioners and FERC mistakenly argue that the Court of Appeals' ruling conflicts with this Court's decision in *Morgan Stanley* because the court rejected the application of *Mobile-Sierra* to non-party challenges on the basis that it would "deprive non-settling parties of their statutory right to have rate challenges adjudicated under the 'just and reasonable' standard." Pet. Br. 25. *See also* FERC Br. 14. The Petitioners state that this Court's decision in *Morgan Stanley* rejected the claim that the public interest standard was "a standard different from the statutory just and reasonable standard," but instead was a "differing application of that statutory just and reasonable standard." Pet. Br. 26 (citing *Morgan Stanley*, 128 S.Ct. at 2740). These arguments elevate form over substance as these concepts played no role in the Court of Appeals' legal conclusions.

In *Morgan Stanley*, this Court observed that the Commission and the Courts of Appeals have used a longstanding nomenclature to refer to the two modes of review under the single, statutory "just and reasonable" standard, language that this Court explicitly recognized did not "stand for the obviously indefensible proposition" the Petitioners now claim the Court of Appeals construed it to mean. *Morgan Stanley*, 128 S.Ct. at 2740. There is nothing in the Court of Appeals' decision below to suggest that the court misunderstood or intended to modify the standard of review. Moreover, the Court of Appeals

did not base its decision on whether the *Mobile-Sierra* presumption was either an extra-statutory standard or an application of the "just and reasonable standard in the contract context." Instead, the court based its decision on the analytically distinct question presented here: whether the *Mobile-Sierra* public interest application of the just and reasonable standard governs rate challenges initiated by non-contracting third parties who are directly affected by the settlement.

Moreover, contrary to the Petitioners' claims, the Court of Appeals' decision below does not upset decades of well-settled precedent. In fact, no court has previously addressed the question of whether the *Mobile-Sierra* doctrine should apply to a challenge to a contract rate brought by an entity that was not a party to the contract. As the Court of Appeals explicitly stated in the decision below: "[i]n the instant case, we are presented with a question of first impression: may the Commission approve a settlement agreement that applies the highly-deferential public interest standard to rate challenges brought by non-contracting third parties?" Pet. App. 20a.

None of the cases cited by the Petitioners conflicts with the proposition set forth by the Court of Appeals that the *Mobile-Sierra* doctrine is applied "to preserve the terms of the bargain *as between the contracting parties*. But when a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply; the

proper standard of review remains the 'just and reasonable' standard in section 206 of the FPA." Pet. App. 22a. For example, in *Boston Edison Co. v. FERC*, 233 F.3d 60 (1st Cir. 2000), the application of *Mobile-Sierra* was to a contract rate agreed to between a utility and its two large wholesale customers. FERC's determination that the rate was unjust and unreasonable *for the two customers that were parties to the contract* improperly failed to apply the public interest standard under the *Mobile-Sierra* doctrine.

The First Circuit reasoned that the parties could have "negat[ed] the protection afforded by *Mobile-Sierra* by providing that the contract rate initially fixed by the parties and filed with FERC could be overridden by FERC at any time under the just and reasonable standard." *Id.* at 66. Since the parties did not agree to override the application of the public interest standard to the contract rate, the court ruled that FERC should not have applied the just and reasonable standard. *Boston Edison* thus does not address the situation at issue here, in which contesting parties could not have "opted out" of application of the *Mobile-Sierra* standard (except by agreeing to a settlement that they opposed).

The Petitioners cite *Northeast Utils. Serv. Co. v. FERC*, 993 F.2d 937 (1st Cir. 1993) (*Northeast I*) and *Northeast Utils. Serv. Co. v. FERC*, 55 F.3d 686, 692 (1st Cir. 1995) (*Northeast II*) for the proposition that "[l]ower courts have long applied *Mobile-Sierra* without regard to a challenger's identity." Pet. Br. 31.

However, the question of whether a non-settling party to a settlement agreement may bring a challenge to a rate derived from that settlement agreement was not addressed in *Northeast I* and *II*.

The Petitioners also cite *Wisconsin Public Power v. FERC*, 493 F.3d 239 (D.C. Cir. 2007), and *Town of Norwood v. FERC*, 587 F.2d 1306 (D.C. Cir. 1978), for the proposition that courts have applied *Mobile-Sierra* regularly to non-parties. Pet. Br. 31-32. These cases also do not stand for the proposition for which they are cited. As the Petitioners acknowledge, these cases involved claims of "undue discrimination" and the question of whether disparities between *Mobile-Sierra* contract rates and rates made available to other non-contracting customers constitute prohibited discrimination. Thus, the decisions in these cases addressed challenges to existing contracts, not on the grounds that the contracts would bind the third-party challengers, but instead upon the grounds that contractual counterparties received more favorable terms and conditions of service than those provided to other non-contracting third parties. *See, e.g.*, *Wisconsin Public Power*, 493 F.3d at 269-275. Unlike here, the contracts in question in the cases upon which Petitioners rely did not purport to bind third parties to take service under their own privately negotiated terms and conditions. Nor did those contracts and the *Mobile-Sierra* protections afforded their parties purport to deprive any third party of its statutory right to challenge any

rate applicable to the third party under the ordinary just and reasonable review.

Finally, there is no consistent FERC practice regarding application of the *Mobile-Sierra* presumption. As FERC acknowledged to the Court of Appeals, FERC has applied the *Mobile-Sierra* presumption to third parties only as far back as 2002. Pet. App. 23a. Until 2002, FERC expressly and repeatedly refused to apply the *Mobile-Sierra* presumption to third parties.[3] The Petitioners point to no evidence that, prior to 2002, FERC was besieged by "hordes" seeking to assert rate challenges. Nor do they make any effort to reconcile FERC's pre-2002 *Mobile-Sierra* policy with their sweeping and erroneous declaration that the Court of Appeals' decision conflicts with decades of practice.

Moreover, FERC's application of the *Mobile-Sierra* presumption to non-contracting third parties since 2002 has been far from uniform. FERC has continued

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[3] For example, in *PJM Interconnection*, 96 FERC ¶ 61,206 at 61,878 (2001), FERC rejected an argument that parties to a contract may "bind not only one another, but also other entities who are not parties to that contract (and did not receive the contractual benefits in exchange for which the parties traded away their right to seek rate changes)." *See also Westar Generating, Inc.*, 100 FERC ¶ 61,255 (2002); *Niagara Mohawk Power Corp.*, 97 FERC ¶ 61,018 (2001); *Turlock Irrigation Dist. and Pacific Gas and Elec. Co.*, 88 FERC ¶ 61,322 (1999); *Montana Power Co.*, 88 FERC ¶ 61,019 (1999); *New England Power Co.*, 81 FERC ¶ 61,281 (1997); *Southern Co. Servs. Inc.*, 67 FERC ¶ 61,080 (1994).

to reject agreements that applied the *Mobile-Sierra* presumption to non-signatories in contested settlement agreements. *See, e.g,. Milford Power Co., LLC*, 119 FERC ¶ 61,167, at 64,032 (2007); *Bridgeport Energy, LLC*, 118 FERC ¶ 61,243 at 62,193 (2007). Just as in the present case, FERC has observed that the purpose of certain types of agreements with generators to provide reliability service have a "wide applicability" to market participants that are much broader in number than the entities executing the agreements. *Id.* In such cases, FERC determined that it was inconsistent with its duty under the FPA to be bound to the restrictive "public interest" mode of review when reviewing such agreements. *Id.* FERC determined that "any challenges to the . . . agreement by non-parties under section 206 of the FPA shall be reviewed by the Commission under the just and reasonable standard." *Milford Power*, 119 FERC ¶ 61,167, at 62,043; *see also Bridgeport Energy*, 118 FERC ¶ 61,243 at 62,194 (2007).

E. The Fpa Does Not Presume That Market-Based Rates Are Reasonable Except With Respect To Challenges By The Contracting Parties Themselves

The Petitioners assert that non-parties should be subject to the *Mobile-Sierra* presumption because market-based rates are presumptively reasonable "in the broader sense of economic efficiency." Pet. Br. 35. That argument does not withstand scrutiny, even

assuming that rates derived from the contested settlement agreement are actual market-based rates (which is not at issue here). The cases that the Petitioners cite do not stand for the proposition that the *Mobile-Sierra* presumption invariably insulates market-based rates from challenge. To the contrary, this Court and Court of Appeals cases have consistently warned FERC against presuming that contracts putatively reflecting market-based transactions naturally yield just and reasonable rates. Neither the Commission nor the courts may presume that "market-based" rates are inherently just and reasonable. *See Tejas Power Corp. v. FERC*, 908 F.2d 998, 1003-05 (D.C. Cir. 1990). Such rates must remain subject to the ordinary just and reasonable standard of review.

This Court has stated that the Commission may not rely upon market-based regimes to produce just and reasonable rates, not because markets are necessarily inefficient, but because Congress and the FPA prohibit it. *See FPC v. Texaco*, 417 U.S. 380, 400 (1974) ("*Texaco*"). Specifically, the Court held that:

> [i]n concluding that the Commission lacks the authority to place exclusive reliance on market prices, we bow to our perception of legislative intent. It may be, as some economists have persuasively argued, that the assumptions of the 1930's about the competitive structure of the natural gas industry, if true then, are no longer true today. It may also be that control of prices in this industry, in a time of shortage, if such

> there be, is counterproductive to the interests of the consumer in increasing the production of natural gas. It is not the Court's role, however, to overturn congressional assumptions embedded into the framework of regulation established by the Act. This is a proper task for the Legislature where the public interest may be considered from the multifaceted points of view of the representational process.

Id. While *Texaco* did not involve an application of the *Mobile-Sierra* doctrine, it is clear that FERC may not rely solely upon market forces to produce just and reasonable rates.

Similarly, in *Farmers Union Central Exchange v. FERC*, 734 F.2d 1486 (D.C. Cir. 1984), *cert. den. sub nom., Williams Pipe Line Co. v. Farmers Union Cent. Exch. Inc.*, 469 U.S. 1034 (1984), the court considered the permissible context for the charging of market-based rates. In that case, FERC presumed that if it established ceiling prices, albeit at very high levels, "market forces could be relied upon to keep prices at reasonable levels throughout the oil pipeline industry." *Id.* at 1510. The court rejected this reasoning, stating that:

> [w]ithout empirical proof that it would, this regulatory scheme, however, runs counter to the basic assumption of statutory regulation, that "Congress rejected the identity between the 'true' and the 'actual' market price." *FPC v. Texaco*, 417 U.S. at 399. In fact, FERC's "'regulation' by such novel 'standards' is

> worse than an *exemption simpliciter*. Such an approach retains the false illusion that a government agency is keeping watch over rates, pursuant to the statute's mandate, when it is in fact doing no such thing." *Texaco v. FPC*, 474 F.2d at 422.

Id.; Cal. ex rel. Lockyer v. FERC, 383 F.3d 1006, 1012-13 (9th Cir. 2004).

As these cases make clear, applying a presumption that rates are reasonable simply because they are market-based would be incompatible with FERC's obligation under the FPA. In the end, if the Petitioners' market theory operated in practice, there would be no need for the FPA or the Natural Gas Act. Congress, however, determined that sellers and buyers in the utility industry may possess market power and hence required FERC review of such contracts to ensure that utility economic power was not used to exploit the public, which is the ultimate purchaser of utility goods and services but is not invited to the bargaining table. It is beyond the authority of the Commission and the courts to alter a statutory scheme of regulation and review simply because certain economists or contracting parties may believe they have a better approach.

III. FERC DOES NOT HAVE "DISCRETION" TO APPLY THE *MOBILE-SIERRA* PUBLIC INTEREST STANDARD AGAINST THIRD PARTIES OUTSIDE THE CONTRACT CONTEXT

Although FERC properly acknowledges that the transition payment rates and auction results are not contracts subject to the *Mobile-Sierra* presumption, FERC argues that it has the discretion to apply the presumption to future challenges to those rates under its broad authority to approve contested settlement agreements that the Commission believes will produce just and reasonable rates. FERC Br. 32. FERC further argues that the regulatory structure for non-parties remains unchanged because the public interest standard is "simply one application of the more general just and reasonable standard." *Id.* This argument is not properly before the Court and fails on its merits.

As an initial matter, the Court should not accept FERC's invitation to decide whether it has the power to impose the public interest standard as a matter of discretion. FERC did not present this theory in its brief in opposition to the petition for a writ of certiorari and did not expressly present this theory to the Court of Appeals. Whether FERC has the far-reaching power to decide unilaterally that ordinary just and reasonable review does not apply to a tariff rate challenge is a significant issue of first impression that should not be raised for the first time

in this Court to justify reversing a Court of Appeals judgment.[4] *See also SEC v. Chenery Corp.*, 318 U.S. 80, 95 (1943) ("an administrative order cannot be upheld unless the grounds upon which the agency acted in exercising its powers were those upon which its action can be sustained").

FERC's argument is also wrong on the merits. This Court stated in *Morgan Stanley* that the public interest standard operates in a contract context. *Morgan Stanley*, 128 S.Ct. 2746. Because the rate at issue is not a contract, *Mobile-Sierra* does not apply *ab initio*. Moreover, outside the context of a contract, the Commission has no authority to vitiate the Section 206 rights of non-contracting parties. If, as FERC acknowledges, there is no contract, any review must be under the ordinary and statutory just and reasonable standard.

FERC's broad authority to approve settlement agreements is circumscribed by the statutory requirement that it must fix rates "upon complaint," on a showing by the complainant that a rate is "unjust, unreasonable, unduly discriminatory, or preferential." 16 U.S.C. § 824e. This mandate would be wholly undermined and circumvented if FERC had discretion to apply a contract-based standard of

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[4] By contrast, the Respondents pressed below and in their brief in opposition that auction results and transition payments are not contracts subject to the *Mobile-Sierra* presumption.

review in a non-contract case. Whereas in a contract context, a party could agree to an unfair rate that may nevertheless be consistent with the public interest, FERC may not impose such a rate absent an agreement. *See Sierra*, 350 U.S. at 354-355.

To permit FERC to apply *Mobile-Sierra* in a non-contract context would in effect ignore the plain language of Section 206 that permits a complainant to seek modification of rates "upon complaint" when the complainant demonstrates that the rates to which it did not agree are unjust. FERC should not be permitted to claim discretion to determine when it will ignore the private interests of complainants and consider only whether the rates pose a grave harm to the public.

Contrary to FERC's claim, the public interest standard is not merely a general application of the just and reasonable standard that provides for the statutory review of claims raised by non-contracting parties. Rather, as noted above, the public interest standard is "the definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context," *Morgan Stanley*, 128 S.Ct. 2746, a context FERC expressly admits is not present.

FERC does not have discretion to establish rebuttable presumptions that form a barrier to Section 206 relief. There is nothing in Section 206 that provides for any shifting of burdens or presumptions other than placing the burden of proof on the complainant to show that a rate is unjust or

unreasonable. FERC has not been delegated authority to raise the barrier to a Section 206 review any higher than that established by Congress. That is the role of Congress, and FERC may not overturn congressionally established provisions of the FPA. *See Texaco*, 417 U.S. at 400.

IV. THE DECISION BELOW DOES NOT VITIATE ANY REASONABLE EXPECTATION OF CONTRACT STABILITY OR THREATEN INDUSTRY STABILITY

The Petitioners' and amici's claim that the right of the non-settling parties to challenge rates that result from the settlement agreement under the ordinary just and reasonable standard will threaten industry stability is without merit and should be rejected. *See* Pet. Br. 37-41; Econ. Br. 18-26; EPSA Br. 19-21. The Petitioners' claim that the "vast field of potential complainants with powerful incentives to upset the agreements," will upset the agreements destroy stability, and reduce the role of *Mobile-Sierra* to a "historical footnote" is grossly exaggerated. *See* Pet. Br. 39-40.

The Petitioners' argument is premised on their concern that any and all non-parties to a contract—*e.g.*, indirectly affected consumers—can now challenge energy contracts under the ordinary standard. Pet. Br. 37. In their view, this effectively vitiates the *Mobile-Sierra* doctrine, which was created to advance stability. But that situation is not

presented here and the Respondents take no position on it. On the narrower issue of challenges by entities that objected to a settlement but are now bound by it, the Respondents' position poses no threat whatsoever to industry stability.

As an initial matter, the settling parties cannot have had a reasonable expectation that their settlement agreement, or the tariff rates resulting from the transition payments and FCM pricing mechanisms that they agreed upon amongst themselves over the objections of the Respondents, would be free from uncertainty. As the Court of Appeals explained, the *Mobile-Sierra* presumption of reasonableness ensures contract stability "*as between the contracting parties*" and "[i]t makes no sense to say that the values of 'stability' and 'certainty' are furthered by applying the deferential standard of review to the eight parties that *refused* to agree to the terms of the settlement." Pet. App. 24a (emphasis in original). Entering into a settlement agreement with some, but not all, parties to a complex multiparty case entails the risk of further litigation.

Upholding the ruling below does not create uncertainty. If settling parties cannot unilaterally bind non-settling parties to their agreement, they still have recourse to compromise other aspects of the settlement with the non-settling parties in order to obtain their consent to limit their rights under Section 206. Alternatively, to the extent that the settling parties value those other aspects of the settlement more than absolute certainty, they may

choose to settle amongst themselves without the consent of all the parties.

The notion that upholding the right of the non-settling parties to challenge the FCM tariff rates under the ordinary just and reasonable standard would cause substantial increases in risk premiums to developers or force developers to abandon development necessary to meet the increasing demand for electricity, *cf.* Pet. Br. at 40, is belied by the fact that even with this supposed litigation uncertainty, for the first three annual capacity auctions, significant amounts of new capacity resources, well in excess of the installed capacity requirement for New England, have qualified to participate in the auctions. At the same time, the annual price determined by the auction mechanism has been moving downward, not upward, and is now below the unreasonably high rates paid to capacity resources during the transition period. To say that ratepayers will be harmed by their own right to challenge these rates is unfounded.

Moreover, the Petitioners' claim that allowing non-settling parties to challenge the settlement agreement under the ordinary just and reasonable standard threatens industry stability is profoundly overstated. As noted above, FERC's "policy" of applying the *Mobile-Sierra* public interest standard to non-parties dates back only as far as 2002, Pet. App. 23a, and since that time has not been applied consistently. The electric industry managed to maintain its stability and integrity for the five

decades of *Mobile-Sierra* jurisprudence before that 2002 policy shift, and since.

The Petitioners cite to forty-one cases before FERC, resolved subsequent to the ruling below, in which the parties included with their *Mobile-Sierra* provisions language that would apply the "most stringent standard permissible," or similar language, to challenges raised by non-parties. Pet. Br. 39; Pet. Reply, App. 1a-10a. The Petitioners maintain, "[t]hat so many thought it desirable to include such provisions confirms that non-party challenges are a real threat." *Id.* At most this tells us that contracting parties will try to bind non-contracting parties if given the opportunity. Parties, however, have continued to enter into agreements, even where *Mobile-Sierra* has not applied to non-parties. Although the new "most stringent standard permissible" language now incorporated into contracts under the ordinary just and reasonable standard is not nearly as restrictive as the "nearly insurmountable" public interest standard under *Mobile-Sierra*, the stability of contract afforded to contracting parties by FERC under the ordinary just and reasonable standard has been sufficient and has not caused uncertainty.

FERC always has an obligation to consider all of the public policy concerns articulated by the Petitioners, including the benefits of contract stability, industry stability, grid reliability and resource adequacy, in resolving any challenge to the settlement tariff rates. FERC also must be free to consider all the other policy concerns any challenger

to the rates might bring, including whether the rates are so high as to constitute a burden to consumers and the regional economy. After all, the "primary aim of this legislation was to protect consumers against exploitation." *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 610 (1944). Therefore, non-contracting ratepayers must always be permitted to show that unfair rates pose a specific harm to them and not be limited to making a showing of a grave public necessity requiring a modification to such rates.

Finally, recognizing that *Mobile-Sierra* does not apply to challenges raised by non-contracting parties does not leave contracts unprotected nor does it upset the reasonable expectations of contracting parties. Non-contracting parties challenging contract rates still have the burden to prove that the terms are unjust and unreasonable, and the Commission has shown restraint in abrogating private contracts unless this fairly high burden is met.

The Respondents would have the burden of showing that the auction rate or the transition payment was unjust and unreasonable. This is as Congress intended. Moreover, this is not an insignificant burden. For example, FERC recently denied a complaint by several regulatory agencies, consumer advocates and consumer interests against PJM Interconnection, LLC. The complainants in that matter asserted that the results of the PJM capacity auction were unjust and unreasonable. FERC denied the complaint finding that the auction elements complained of were part of the Reliability Pricing

Model ("RPM") that was incorporated into the provisions of the PJM tariff and that there was no allegation that PJM had violated these tariff provisions. *Maryland Public Service Commission v. PJM Interconnection, LLC,* 124 FERC ¶ 61,276, 62,562 (2008). On rehearing, FERC affirmed its dismissal of the Complaint stating that "as we found in the September Order, while revisions to RPM may be appropriate for the future, RPM Buyers have not made a sufficient showing to justify upsetting already-conducted auctions." *Id.* at 62,559.

Thus, simply filing a Complaint would not result in an overturning of the transition or auction rates established by tariff pursuant to the contested settlement agreement. Instead, under the applicable just and reasonable standard under Section 206 of the FPA, the Respondents or any other party would have to clear a high hurdle to show that the rates had become unjust and unreasonable. Parties operating in the public utility arena well know that unjust and unreasonable rates may be set aside and hence there is no violence to their contractual expectations to hold them to such a standard.

CONCLUSION

For the foregoing reasons, the judgment of the Court of Appeals should be affirmed.

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REPLY BRIEF

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No. 08-674

In the Supreme Court of the United States

NRG POWER MARKETING, LLC, ET AL., PETITIONERS

v.

MAINE PUBLIC UTILITIES COMMISSION, ET AL.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

REPLY BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION

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REPLY BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION

In the order at issue in this case, the Federal Energy Regulatory Commission (Commission or FERC) approved a comprehensive settlement of a long-running dispute concerning the structure of the market for electric generating capacity in New England. Section 4.C of the settlement provides that future challenges to certain rates established pursuant to the settlement will be governed by the "public interest" standard of review described in *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956) (*Mobile*), and *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956) (*Sierra*). J.A. 95. The Commission reasonably exercised its discretion in approving the settlement, including the public-interest review provision of Section 4.C. The court of appeals erred in setting aside FERC's order, and its judgment should be reversed.

Petitioners criticize the reasoning of the court of appeals, while the non-FERC respondents attempt to defend the court's decision, but largely on grounds other than those on which it relied. Petitioners are correct in their ultimate conclusion that the judgment below should be reversed and FERC's order upheld. But neither petitioners nor respondents accurately describe what the Commission did in its order. And neither petitioners nor respondents focus on the central issue in this case, which is the reasonableness of the Commission's decision to approve the settlement, and, in so doing, to specify the manner in which it would carry out its statutory obligation to ensure just and reasonable rates. See 16 U.S.C. 824d, 824e.

Petitioners argue (Br. 47) that the rates covered by Section 4.C of the settlement agreement are the product of "contracts protected by *Mobile-Sierra*," so that Section 4.C "merely recited the standard that would apply in any event." That is incorrect. The rates to which Section 4.C applies—the results of the forward capacity auctions conducted under the settlement and the transition payments specified in the settlement—are generally applicable tariffs. They are not contract rates to which *Mobile* and *Sierra* would apply of their own force, and even if they were, the Commission could have required the settling parties to forgo the protections of *Mobile* and *Sierra* as a condition of its approval of the settlement. In other words, the public-interest standard is relevant to this case not because *Mobile* and *Sierra* are controlling, but only because the Commission made a discretionary decision to apply that standard.

Respondents, for their part, make an error in the opposite direction. Beginning with the correct premise that "the rates produced by the settlement are not 'con-

tract rates' to which the *Mobile-Sierra* presumption could apply," they assert that FERC lacked authority to "rewrite the terms of the" Federal Power Act (FPA), 16 U.S.C. 791a *et seq.*, and "abrogate the Respondents' statutory rights" by approving a settlement calling for application of the public-interest standard of review. Br. 11, 14. That reasoning is flawed because it overlooks that the underlying statutory requirement that rates be "just and reasonable," 16 U.S.C. 824d(a), does not compel the Commission to pursue any single regulatory approach. Respondents fail to appreciate that the "public interest standard" is not separate from—still less an "abrogat[ion]" of—the statutory just-and-reasonable standard, but is merely one way to implement that standard. See *Morgan Stanley Capital Group Inc.* v. *Public Util. Dist. No. 1*, 128 S. Ct. 2733, 2740 (2008) (*Morgan Stanley*).

Having carefully reviewed the settlement, the Commission determined that the auction mechanism would produce just and reasonable rates and that the transition payments were also just and reasonable. Based on those findings, and taking into account the interests in ensuring an adequate supply of generating capacity by promoting market stability, the Commission decided to approve the use of the public-interest standard as specified in Section 4.C. Significantly, although respondents essentially ignore the point, Section 4.C provides for application of the general just-and-reasonable standard—not the particular public-interest standard—to any future challenge to the rules that govern the conduct of the auctions, as well as to the rates produced by each auction during the 45 days after those rates are filed with the Commission. The Commission's approach, in all of these respects, was reasonable.

The foregoing reasons provide a sufficient basis for reversing the judgment of the court of appeals. But the court also erred in another respect, by holding that the application of the public-interest standard under *Mobile* and *Sierra* is limited to challenges brought by the contracting parties. That holding rests on a misunderstanding of *Mobile* and *Sierra*, and respondents' efforts to defend it are unavailing. If under *Mobile* and *Sierra*, the public-interest standard were statutorily mandated here—which it is not—then that standard would govern all challenges to the rates set by contract, regardless of the identity of the challenger.

A. The Commission Was Not Required To Approve The Settlement As A Whole Or Section 4.C In Particular

Section 4.C of the settlement provides that "the standard of review for: (i) challenges to the Capacity Clearing Prices derived through the [Forward Capacity Market] and * * * (ii) proposed changes to Section 11, Part VIII below (Agreements Regarding Transition Period) and the Market Rules implementing that part, shall be the 'public interest' standard of review" described in *Mobile* and *Sierra*. J.A. 95. Petitioners argue (Br. 47) that Section 4.C "merely recited the standard that would apply in any event." That is so, they say (*ibid.*), because "[t]he results of the capacity auctions are clearly contracts—voluntary agreements for the sale of capacity between sellers and buyers," and the transition payments "are likewise contract rates" because they "are expressly set forth in a contract" (*i.e.*, the settlement agreement).

Petitioners are correct that the Commission is required "to apply the *Mobile-Sierra* presumption in its evaluation of" rates set by contract. *Morgan Stanley*,

128 S. Ct. at 2745. But petitioners' characterization of the auction results and the transition payments as contract terms is not correct. Moreover, to the extent petitioners suggest that the Commission was required to approve Section 4.C, that is also incorrect: regardless of the nature of the rates covered by Section 4.C—that is, regardless whether they are properly viewed as contract rates or tariff rates—the Commission had the discretionary authority to approve or reject both the settlement of the proceeding as a whole and its provision for public-interest review of those rates.

1. Petitioners' argument that the auction results are contract rates rests on the general proposition that auctions result in contracts between the buyer and seller of the property auctioned. Petitioners refer to the usual auction setting, in which the ultimate agreement for sale of the property auctioned indeed has the hallmarks of a conventional contract. See, *e.g.*, *In re GWI PCS 1 Inc.*, 230 F.3d 788, 807 (5th Cir. 2000) ("General principles of auction law provide a baseline rule that the close of an auction—the fall of the hammer—signals acceptance of the offer and creates a binding contract between the seller and the high bidder."), cert. denied, 533 U.S. 964 (2001); *Lawrence Paper Co.* v. *Rosen & Co., Inc.*, 939 F.2d 376, 379 (6th Cir. 1991).

Contrary to petitioners' assertions (Br. 48-50), however, the forward capacity auction created by the settlement bears little resemblance to a conventional auction. The "demand" side of each annual auction is set not by the load-serving entities who will ultimately pay for capacity, but by the Independent System Operator (ISO) New England, which determines the estimated amount of capacity—known as the installed capacity requirement (ICR)—that the system as a whole will require for

reliability three years in the future. J.A. 121-123; see *Connecticut Dep't of Pub. Util. Control* v. *FERC*, 569 F.3d 477, 480 (D.C. Cir. 2009) (describing the auction mechanism), petition for cert. pending, No. 09-277 (filed Sept. 3, 2009). The ISO New England then announces the auction starting price, which is initially twice the estimated cost of new entry, and capacity providers state how much capacity they would be willing to offer at that price. J.A. 130-131. If capacity providers offer more capacity than required to meet the ICR, the ISO New England lowers the offering price using a "descending clock" process; that process in turn results in a lowering of the quantity of capacity offered until the quantity offered equals the ICR. J.A. 131-132. The ISO New England then assesses each utility in the system a capacity charge equal to the utility's share of the ICR multiplied by the market clearing price. *Connecticut Dep't of Pub. Util. Control*, 569 F.3d at 480.

Thus, the utilities "buying" capacity in the forward capacity market have no input into or role in the auction at all, and cannot be said to be "contracting" with the capacity sellers. Rather than agreeing to pay a specific seller an amount set by a voluntary bid for a particular property—as in a conventional auction—the "buyers" in the capacity auction are assessed a standard rate, based upon the intersection of the ICR set by the ISO New England and the offers made by the capacity sellers to provide capacity. While the bids of the capacity sellers commit them to supply the amount they offer at the clearing price, there are no "voluntary agreements" (Pet. Br. 49) of any sort between them and the buyers of the capacity provided. To the contrary, the standard capacity charge paid by each utility in the system for its share of the ICR is more akin to a conventional cost-

based tariff rate than to any voluntary agreement between that utility and a capacity seller.

2. Petitioners correctly point out (Br. 53) that "the transition-payment obligations *of the settling parties* are clearly 'contract rates'" because the settlement, once approved by the Commission, is at least in part a contract among the settling parties. As to the non-settling parties, petitioners say (Br. 54 n.15) that whether the transition-payment obligations are contract rates is a "complex question[]." But a contractual obligation can only arise from a promise, see Restatement (Second) of Contracts § 1 (1981), and therefore a non-settling party's obligation to make a transition payment—an obligation to which it has never agreed—cannot be said to be based on a contract. Instead, non-settling parties have an obligation to make transition payments because the Commission has approved the settlement prescribing those payments, which therefore are properly viewed as tariff rates.

According to petitioners (Br. 54 n.15), "the settlement does not in fact directly impose transition-payment obligations on non-parties," because the payments are actually made by the independent system operator. That is incorrect. The independent system operator calculates the amounts due and receives and processes the payments, but the payments are made by load-serving entities. Specifically, the settlement provides that transition "[p]ayments will be made to [unforced capacity] entitlement holders," that is, generators, "and made by [unforced capacity] obligation holders," that is, load-serving entities, of which respondent NSTAR Electric and Gas Corporation—an objector to the settlement—is one. J.A. 163; see J.A. 183 (defining "unforced capacity").

3. Finally, even if the auction results and transition payments were contract rates for any of the reasons petitioners offer, it would not follow that the Commission was required to approve Section 4.C of the settlement, which specifies that future challenges to those results and payments shall be governed by the public-interest standard. Petitioners appear to concede that, because the settlement was intended to resolve a contested proceeding before the Commission, the settlement could not become effective until the Commission reviewed it and determined that it was just and reasonable. Pet. Br. 12; J.A. 43; see *Mobil Oil Corp.* v. *FPC*, 417 U.S. 283, 312-314 (1974); 18 C.F.R. 385.602(h). That approval required the exercise of independent judgment by the Commission. And it necessitated an assessment of the likely workings and effect of the settlement, including its auction mechanism and transition-payment framework, on all participants in the New England capacity market, including those who objected to the settlement. Thus, had the Commission believed that the overall settlement was not just and reasonable, it could have refused to approve it, or it could have approved it on the condition that it be modified in some way, such as by requiring that all future challenges to rates be subject to the ordinary just-and-reasonable standard of review.* For this reason as well, the FPA did not compel FERC to approve application of the public-interest standard to the rates at issue in this case.

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* Even in an ordinary contract situation, outside the context of a settlement, the parties may agree to a so-called "*Memphis* clause" specifying that the Commission may review future challenges to the rates under the ordinary just-and-reasonable standard. See *Morgan Stanley*, 128 S. Ct. at 2739; *United Gas Pipe Line Co.* v. *Memphis Light, Gas & Water Div.*, 358 U.S. 103 (1958).

B. The Commission Had Discretion To Approve The Settlement, Including Section 4.C

In approving Section 4.C of the settlement, the Commission specified the standard that it would apply in evaluating future complaints about the rates set by the capacity auctions or the transition payments fixed by the settlement. Those complaints would invoke FERC's authority under 16 U.S.C. 824e(a) to set aside rates that are "unjust, unreasonable, unduly discriminatory or preferential," as well as its authority under 16 U.S.C. 824d(a) to ensure that "[a]ll rates and charges * * * shall be just and reasonable." Accordingly, the Commission's approval of Section 4.C—including its provision for the public-interest standard of review—represented an interpretation of those provisions. That interpretation is a permissible construction of ambiguous statutory language, and respondents' challenges to it lack merit.

1. As an initial matter, respondents assert (Br. 37-38) that this Court should not consider "whether [FERC] has the power to impose the public interest standard as a matter of discretion" because FERC has raised the issue "for the first time in this Court." That suggestion is unfounded. In fact, the Commission has explained, at every stage of these proceedings, that its approval of Section 4.C represented an exercise of its interpretive discretion.

In its order approving the settlement, the Commission did not regard itself as compelled by *Mobile* and *Sierra* to apply the public-interest standard of review to the rates identified in Section 4.C. Instead, the Commission stated that it had "broad authority and discretion * * * to address contested settlements," Pet. App. 133a, and explained that it was approving the proposed settlement only after finding that the proposal was

"consistent with the public interest," *id.* at 135a, and "achieve[d] an overall just and reasonable result," *id.* at 141a-142a. With respect to Section 4.C in particular, the Commission did not say that application of the public-interest standard of review to future challenges to rates was required, but rather that it would be "fully consistent with current Commission policy." *Id.* at 201a; see *ibid.* ("[W]e find this *Mobile-Sierra* provision reasonable.").

Likewise, in its brief before the court of appeals, FERC argued that it had "reasonably exercised its discretion to accept the limited *Mobile-Sierra* provision in the Settlement." FERC C.A. Br. 22; see *id.* at 54 ("Reasonably exercising its discretion, the Commission rejected arguments that it revise or eliminate [Section 4.C], explaining that it is fully consistent with Commission policy, does not operate to the detriment of non-settling parties, and appropriately balances the need for rate stability with the legal requirement that rates be just and reasonable."). The court of appeals, as described earlier, did not consider the Commission's view that it had permissibly interpreted Sections 824d and 824e in approving the settlement.

According to respondents (Br. 37-38), because the court of appeals did not consider the Commission's discretion to specify an appropriate standard of review for rates not governed by *Mobile* and *Sierra*, this Court should not do so either. But since respondents have urged the Court to affirm the judgment below on the alternative ground that "the rates produced by the settlement are not 'contract rates' to which the *Mobile-Sierra* presumption could apply" (Br. 11), they can hardly ask the Court to ignore the question whether there is another basis for applying the public-interest

standard. Indeed, respondents' brief in opposition framed the question presented as "[w]hether the Commission may * * * approv[e] a settlement agreement that would require rate challenges brought by non-settling third parties to be evaluated under the * * * 'public interest' mode of review," Br. in Opp. i—a question that surely encompasses whether the Commission had discretion to prescribe that standard of review.

2. On the merits, respondents' argument rests (Br. 38) primarily on the assertion that "the Commission has no authority to vitiate the [Section 824e] rights of non-contracting parties." That is true, but it begs the question, because respondents do not explain how the application of the public-interest standard could "vitiate" their statutory rights. To the contrary, this Court has held that the public-interest standard is not "different from the statutory just-and-reasonable standard," but rather is only an application of it. *Morgan Stanley*, 128 S. Ct. at 2740. And the Commission recognized in its order that courts have "rejected the notion * * * that the public interest standard is 'practically insurmountable,'" so that "even under the 'public interest' standard of review, the Commission retains significant authority to protect non-parties to the settlement from harm." Pet. App. 202a (quoting *Northeast Utils. Serv. Co.* v. *FERC*, 55 F.3d 686, 691 (1st Cir. 1995)).

Similarly flawed is respondents' contention (Br. 39) that application of the public-interest standard "in a non-contract context would in effect ignore the plain language" of the FPA. The Act says only that rates must be "just and reasonable," and does not specify the manner in which that requirement will be implemented in any particular context. For that reason, this Court has held that the Commission is not "bound to any one

ratemaking formula" and that courts should "afford great deference to the Commission in its rate decisions." *Morgan Stanley*, 128 S. Ct. at 2738; see FERC Br. 24. Given the flexibility inherent in the just-and-reasonable standard, the Commission may require varying types and degrees of justification for the institution of or challenges to particular rates or practices, depending on the circumstances. When rates are set by contract, *Sierra* requires that the Commission apply the public-interest standard. But nothing in the FPA or in this Court's cases precludes the Commission from applying a similar standard of review to other rates as a matter of discretion, if considerations relevant to what is "just and reasonable" make that approach appropriate. Because "Congress has not directly addressed the precise question at issue" here—the standard of review that FERC must apply to future complaints about the capacity-auction results and the transition payments established by the settlement—FERC's interpretation of the just-and-reasonable standard must be upheld as long as it is reasonable. *Chevron U.S.A. Inc.* v. *NRDC*, 467 U.S. 837, 843 (1984). Nor can FERC be faulted for announcing in advance the methodology it will apply in considering future challenges to rates that are produced by the rate-setting methodology it has approved, to promote the interests of transparency and stability in the market.

3. Respondents also contend (Br. 39) that "FERC does not have discretion to establish rebuttable presumptions that form a barrier to [Section 824e] relief." But all FERC has done is to apply the public-interest standard, which this Court has held is required in some circumstances. In any event, the FPA does not prohibit FERC from using appropriate presumptions to guide its decisionmaking. Accordingly, courts have affirmed

FERC's adoption and application of evidentiary presumptions under the FPA and parallel provisions of the Natural Gas Act, 15 U.S.C. 717 *et seq.* See, *e.g.*, *Midcoast Interstate Transmission, Inc.* v. *FERC*, 198 F.3d 960, 970-972 (D.C. Cir. 2000); *East Tenn. Natural Gas Co.* v. *FERC*, 863 F.2d 932, 938 (D.C. Cir. 1988); *Associated Gas Distrib.* v. *FERC*, 824 F.2d 981, 1030-1037 (D.C. Cir. 1987), cert. denied, 485 U.S. 1006 (1988); cf. *Western Res., Inc.* v. *Surface Transp. Bd.*, 109 F.3d 782, 788 (D.C. Cir. 1997) ("The use of presumptions that capture reality in the general run of cases enables the Commission to do its work efficiently, and we have, on a number of occasions, approved its reliance on them."). And as explained below, the Commission's careful review of the settlement gave it ample reason to believe that the auction mechanism and the results it was designed to produce, as well as the transition payments, would be just and reasonable.

C. The Commission Acted Reasonably In Approving The Settlement

The Commission's approval of Section 4.C of the settlement represents a reasonable application of the FPA's requirement that rates be just and reasonable. Section 4.C is just one part of a larger settlement "contain[ing] several complex and interrelated features" that the Commission considered "as a package" and determined would "achieve[] an overall just and reasonable result." Pet. App. 140a-142a. In reaching that conclusion, the Commission found that the settlement would "provide[] the appropriate market structure to ensure that generating resources are appropriately compensated" and that it would "provide[] incentives to attract new infrastructure where needed." *Id.* at 142a. The

Commission emphasized that the settlement had attracted "broad-based support" and would resolve a "difficult, contentious proceeding." *Id.* at 143a. The Commission also made specific findings as to the justness and reasonableness of Section 4.C. *Id.* at 200a-203a. Respondents have not shown that any of those findings was not supported by substantial evidence or that the Commission's ultimate determination was arbitrary and capricious. See 16 U.S.C. 825*l*(b).

1. The Commission reasonably approved Section 4.C's application of the public-interest standard to any challenges brought, after an initial 45-day period, to the prices set by the forward capacity auctions created by the settlement. Even though those auctions result in tariff rates, not contracts between buyers and sellers, see pp. 5-7, *supra*, they nevertheless share with contracts certain market-based features that make the protection for market stability afforded by the public-interest standard appropriate.

Respondents argue (Br. 34) that FERC may not simply "presum[e] that contracts putatively reflecting market-based transactions naturally yield just and reasonable rates." But the Commission did not do so here. Instead, it carefully examined the design of the proposed auctions and determined that they would produce prices that are just and reasonable. See Pet. App. 142a ("[T]he key price-determining parameters of the [forward capacity market] descending clock auction * * * are appropriate and adequately supported in the record."); *id.* at 161a-193a (considering, and rejecting, objections to specific aspects of the auction design). Respondents make no effort to challenge those findings.

Significantly, moreover, the public-interest review provision of Section 4.C does not apply to "the market

rules that will be developed and filed with the Commission under the Settlement Agreement." Pet. App. 200a. Should any party develop grounds to contend that the auction rules are not producing just and reasonable prices, the Commission can alter the rules as appropriate, entirely unrestricted by Section 4.C. See *id.* at 78a.

The Commission also made sure that it will be able to monitor, on an ongoing basis, how the auctions work in practice, so that it will be in a position to modify the market rules if necessary and review the rates set under the auction each year. The settlement requires the ISO New England to make an informational filing with the Commission before each auction. Pet. App. 202a. It further requires the ISO New England to file the results of the auction with the Commission, after which they will be subject to challenge for 45 days. *Ibid.*; J.A. 118-119. Should any party believe that the results of an auction are not just and reasonable, it will be free to challenge them—unrestricted by Section 4.C—so long as it does so within that period. In light of those safeguards, the Commission reasonably concluded that, following the 45-day period, application of the public-interest standard to the results of the auction would be appropriate—especially since the rates set by an auction are in effect for a period of only one year, after which they will be reset by the rates determined in the next annual auction. All FERC has done is take the modest step of imposing a 45-day statute of limitations on bringing an ordinary just-and-reasonable challenge to the rates set by auction for the New England capacity market. The interests in repose and stability, which are critical for the smooth functioning of the auction mechanism, amply justify that limitation. And, of course, a load-serving utility may always choose to bypass the auction system

and acquire its assured capacity by bilateral contract, through the self-supply option the settlement agreement preserves. Pet. App. 112a-113a; see J.A. 84-85.

2. Section 4.C also applies the public-interest standard to future challenges to the payments prescribed in the settlement for the three-year transition period lasting until the auction-based capacity market becomes fully operational. As explained in FERC's opening brief (at 39), the Commission reviewed those payments and found them to be just and reasonable, and the court of appeals agreed. Pet. App. 144a-161a; *id.* at 8a-19a. Respondents do not contend that the likelihood of changed circumstances within the transition period was or is so great that revision of the rates would become appropriate. See J.A. 163. Having reviewed the transition payments at their inception, the Commission reasonably determined that a party seeking to be relieved from those payments should have to show that they were impairing the public interest. Respondents have made no effort to challenge the Commission's conclusion on that point.

3. One important factor that the Commission considered in deciding whether to apply the public-interest standard to the auction results and transition payments was the interest in encouraging investment by protecting industry stability. "Stability is particularly important in this case," the Commission found, because New England has suffered capacity shortages as a result "of the unstable nature of [capacity] revenues and the effect that has on generating units, particularly those who are critical to maintaining reliability." Pet. App. 202a; see *id.* at 78a-79a. As this Court has recognized, the public-interest standard of review is "a key source of stability." *Morgan Stanley*, 128 S. Ct. at 2749. In the context of

the auction results, certainty is important to suppliers of capacity, who must make immediate investments but will not actually deliver capacity at the rates set by the auctions until three years in the future. J.A. 62. Similarly, FERC noted that the transition payments "require a long-term commitment" from suppliers of capacity and "add certainty and price stability for load customers." Pet. App. 158a-160a.

Respondents argue (Br. 42) that concerns about stability in the New England capacity market are "overstated," but, as the court of appeals has elsewhere recognized, "[p]redictions regarding the actions of regulated entities are precisely the type of policy judgments that courts routinely and quite correctly leave to administrative agencies." *Public Utils. Comm'n* v. *FERC*, 24 F.3d 275, 281 (D.C. Cir. 1994); accord *FCC* v. *National Citizens Comm. for Broad.*, 436 U.S. 775, 813-814 (1978); see *Marsh* v. *Oregon Natural Res. Council*, 490 U.S. 360, 378 (1989) ("When specialists express conflicting views, an agency must have discretion to rely on the reasonable opinions of its own qualified experts even if, as an original matter, a court might find contrary views more persuasive.").

D. The Court Of Appeals Erred In Holding That The *Mobile-Sierra* Doctrine Is Inapplicable To Third-Party Challenges To Contract Rates And Terms

Separate and apart from declining to recognize the Commission's discretion to apply the public-interest standard to the transition payments and auction rates, the court of appeals also erred in limiting application of the public-interest standard under the (non-discretionary) *Mobile-Sierra* doctrine to challenges raised by contracting parties. According to the court, "the *Mobile-*

Sierra doctrine is designed to ensure contract stability *as between the contracting parties—i.e.* to make it more difficult for either party to shirk its contractual obligations." Pet. App. 24a. By contrast, "when a rate challenge is brought by a non-contracting third party," the court stated, "the *Mobile-Sierra* doctrine simply does not apply." *Id.* at 22a. In such a case, the court held, "the proper standard of review remains the 'just and reasonable' standard" of Section 824e. The court of appeals misunderstood *Mobile* and *Sierra*, and that error provides an independent basis for reversing the court's judgment. Respondents' efforts to defend the court's reasoning are unavailing.

1. As explained in FERC's opening brief (at 17-22), the court of appeals' interpretation of *Mobile* and *Sierra* was flawed for three reasons. First, the court failed to appreciate that the *Mobile-Sierra* doctrine rests on a "presum[ption] that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law." *Morgan Stanley*, 128 S. Ct. at 2737; see *Verizon Commc'ns Inc.* v. *FCC*, 535 U.S. 467, 479 (2002) (*Verizon Commc'ns*). In other words, the *Mobile-Sierra* presumption applies because of the process by which the rate was set—a freely negotiated contract—not because of the identity of the party challenging the rate.

Second, the essential point of the *Mobile-Sierra* public-interest standard is to allow the Commission to modify rates when doing so is necessary to protect third parties. See *Morgan Stanley*, 128 S. Ct. at 2746 ("[O]nly when the mutually agreed-upon contract rate seriously harms the consuming *public* may the Commission declare it not to be just and reasonable.") (emphasis added); see *Verizon Commc'ns*, 535 U.S. at 479. It there-

fore makes little sense to exclude challenges by "non-contracting third part[ies]," Pet. App. 22a, from the application of that standard.

Third, the rule adopted by the court of appeals would make the Commission's power to enforce Section 824e dependent upon the filing of a complaint by a third party. If, acting on its own motion, FERC initiated an investigation into a contract rate, it would be able to set aside the rate only if it found that the rate was harmful to the public interest. See *Papago Tribal Util. Auth.* v. *FERC*, 723 F.2d 950, 934 (D.C. Cir. 1983), cert. denied, 467 U.S. 1241 (1984). But if the Commission's investigation were triggered by a complaint filed by any person other than the contracting parties, the rate would be reviewed under the ordinary just-and-reasonable standard. Nothing in the FPA or this Court's cases suggests that the scope of the Commission's authority should be dependent on whether a complaint is filed.

2. Respondents attempt to defend the court of appeals' conclusion by arguing that "a prerequisite to the application of the *Mobile-Sierra* doctrine is a willing buyer and a willing seller." Br. 20 (capitalization modified). That premise is correct, in that the *Mobile-Sierra* doctrine governs the review of rates set by contract, and the existence of a willing buyer and a willing seller is a prerequisite to the formation of a contract. But it does not follow that the limited public-interest standard of review under *Mobile-Sierra* applies only to later challenges brought by the buyer or the seller.

According to respondents, application of the public-interest standard is appropriate only with respect to parties who "*agree* to give up a right to challenge" contract rates. Br. 23; see *id.* at 22 ("[T]he *Mobile-Sierra* doctrine restricts the ability of a contracting party to

seek regulatory relief from the obligations to which it agreed in the contract."); *ibid.* ("*Mobile-Sierra* addresses the relationship between parties to a contract."). That reasoning repeats the error of the court of appeals, which believed that the function of *Mobile-Sierra* is "to make it more difficult for either party [to a contract] to shirk its contractual obligations." Pet. App. 24a. But this Court in *Morgan Stanley* emphatically rejected the proposition that *Mobile-Sierra* is "the equivalent of an estoppel doctrine." 128 S. Ct. at 2746 (citation omitted). *Morgan Stanley* held that *Mobile* and *Sierra* do not rest on the premise that the contracting parties are estopped from challenging a rate to which they have agreed, but rather on a "presum[ption] that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law." *Id.* at 2737. That presumption is unaffected by the identity of the person bringing the challenge.

3. Respondents assert (Br. 25-27), in support of the court of appeals' holding, that they are "directly" affected by the rates subject to the *Mobile-Sierra* clause at issue in the settlement. In their view (Br. 26), those rates effectively determine "the rates charged to the Respondents for wholesale service." But even if that claim is true, the court of appeals' decision is not limited to third parties who are "directly," as opposed to "indirectly," affected by a *Mobile-Sierra* contract. Instead, the court of appeals held as a categorical matter that *Mobile-Sierra* "simply does not apply" "when a rate challenge is brought by a non-contracting third party." Pet. App. 22a. That statement is incorrect.

In any event, the identity of respondents here provides an additional reason for the public-interest standard to apply to their challenges. Only respondent

NSTAR Electric and Gas Corporation is a wholesale purchaser of capacity. None of the other respondents participates directly in the New England capacity market. They are, rather, two coalitions of industrial consumers and a group of state officials, who presumably are interested in protecting retail customers who consume power from participants in the wholesale market. Under the framework of the FPA, state regulation of retail rates must take as a given the wholesale rates established under the FPA, whether by contract or by tariff. See, *e.g.*, *Nantahala Power & Light Co.* v. *Thornburg*, 476 U.S. 953 (1986). It therefore would be contrary to the framework of the entire Act, not merely the *Mobile-Sierra* rule and *Morgan Stanley*, to allow a collateral attack on the wholesale contract rate by third-party retail customers under a standard different from the standard that applies when one of the contractual parties seeks to change the rate.

4. Finally, respondents suggest (Br. 32-33) that FERC has been inconsistent in its application of *Mobile-Sierra*. In its order, FERC acknowledged that, before 2002, it had not applied *Mobile-Sierra* to third-party challenges, but explained that it had changed its approach. Pet. App. 77a. Respondents do not argue that the change was procedurally defective or inadequately explained, nor could they plausibly do so. See generally *FCC* v. *Fox Television Stations, Inc.*, 129 S. Ct. 1800, 1810-1812 (2009).

Instead, respondents assert (Br. 32) that, even after 2002, "FERC's application of the *Mobile-Sierra* presumption to non-contracting third parties * * * has been far from uniform." That is incorrect. The cases they cite, *Milford Power Co., LLC*, 119 F.E.R.C. ¶ 61,167 (2007), and *Bridgeport Energy, LLC*,

118 F.E.R.C. ¶ 61,243 (2007), involved the ability of parties to bind the Commission to public-interest review of reliability-must-run (RMR) agreements. An RMR agreement entitles a generator to recover its full cost-of-service rate rather than the rate it could obtain on the open market. See *Blumenthal* v. *FERC*, 552 F.3d 875, 878 (D.C. Cir. 2009). Such agreements help to maintain reliable supply by keeping high-cost generators in operation, but they interfere with the efficient functioning of a competitive market. *Ibid.*

In *Bridgeport* and *Milford*, the Commission found that RMR agreements suppress market-clearing prices, deter investment in new generating capacity, and require many market participants to pay out-of-market prices for service, hindering market development and performance. *Bridgeport*, 118 F.E.R.C. at 62,193; *Milford*, 119 F.E.R.C. at 62,042; Pet. App. 215a; *id.* at 81a-82a. As a result, the Commission determined that RMR agreements should be used only as a last resort, and announced that it would not be bound by the public-interest standard in reviewing such agreements. *Bridgeport*, 118 F.E.R.C. at 62,193; *Milford*, 119 F.E.R.C. at 62,042. The decisions in *Milford* and *Bridgeport* turn on the market-disrupting effects of RMR agreements, not on any distinction between third-party challenges and other challenges. *Id.* at 62,042 n.47; *Bridgeport*, 118 F.E.R.C. at 62,193 n.30. Those decisions therefore have no relevance here.

* * * * *

For the foregoing reasons and those stated in the opening brief, the judgment of the court of appeals should be reversed insofar as it granted the petitions for review.

Respectfully submitted.

ELENA KAGAN
Solicitor General

OCTOBER 2009

REPLY BRIEF

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IN THE

Supreme Court of the United States

NRG POWER MARKETING, LLC, *ET AL.*,
Petitioners,

v.

MAINE PUBLIC UTILITIES COMMISSION, *ET AL.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

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CORPORATE DISCLOSURE STATEMENT

Pursuant to this Court's Rule 29.6, petitioners NRG Power Marketing, LLC, Devon Power LLC, Connecticut Jet Power LLC, Norwalk Power LLC, Middletown Power LLC, Montville Power LLC, and Somerset Power LLC state that the corporate disclosure statement included in petitioners' opening brief remains accurate.

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IN THE

Supreme Court of the United States

No. 08-674

NRG POWER MARKETING, LLC, *ET AL.*,
Petitioners,

v.

MAINE PUBLIC UTILITIES COMMISSION, *ET AL.*,
Respondents.

On Writ of Certiorari
to the United States Court of Appeals
for the District of Columbia Circuit

REPLY BRIEF FOR PETITIONERS

For more than 50 years, the *Mobile-Sierra* doctrine has preserved "the stability of supply arrangements which all agree is essential to the health of the * * * industry," *United Gas Pipe Line Co.* v. *Mobile Gas Serv. Corp.*, 350 U.S. 332, 344 (1956), by requiring FERC to "presume" that contract rates meet "the 'just and reasonable' requirement imposed by law," and permitting FERC to abrogate such rates only in "extraordinary circumstances where the public will be severely harmed," *Morgan Stanley Capital Group Inc.* v. *Pub. Util. Dist. No. 1*, 128 S. Ct. 2733, 2737, 2749 (2008). Respondents do not dispute that the decision below creates a broad exception to that rule, allowing *everyone* from the virtually

unlimited ranks of indirectly affected non-contracting parties—whether retail consumers, interest groups, state regulators, or elected officials—to challenge contract rates free from *Mobile-Sierra*'s requirements. That decision would render half a century of *Mobile-Sierra* jurisprudence a pointless exercise. *Mobile-Sierra* would preserve the Federal Power Act's principle of contract stability in challenges by contracting counterparties but abandon it whenever the challenge came from anyone else. That decision cannot be reconciled with the rationales underlying *Mobile-Sierra*. It cannot be reconciled with *Morgan Stanley*. And it cannot be reconciled with common sense.

Despite having successfully urged the court of appeals to adopt precisely the broad exception it adopted, see Resp. C.A. Br. 51-53, respondents now defend that holding at best half-heartedly and then quickly shift to alternative theories. Respondents first propose a narrower challenger-based exception, claiming that—even if *Mobile-Sierra* applies to non-parties generally—it should not apply here because respondents are not typical non-parties. Alternatively, they claim that *Mobile-Sierra* does not apply because the rates at issue are not contract rates. But this Court granted review to address the issue the court of appeals decided: "Whether *Mobile-Sierra*'s public-interest standard applies when a contract rate is challenged by *an entity that was not a party to the contract*." Pet. i (emphasis added). It did not grant review to consider whether some other putatively special category of challengers should be exempt, or whether the particular rates here should be exempt.

Neither alternative theory supports the judgment below in any event. Respondents, for example, urge that they should be allowed to challenge the rates at issue

without regard to *Mobile-Sierra* because, unlike typical "indirectly affected" non-parties, they are purportedly "b[ou]nd" by the settlement to "pay certain rates." Resp. Br. 20. That theory would require the Court to *modify* the judgment, not affirm it. The court of appeals held that the settlement agreement's *Mobile-Sierra* clause could not be applied to *any* non-contracting party, not just respondents: "[W]hen a rate challenge is brought by a non-contracting third party," the court held, "the *Mobile-Sierra* doctrine simply does not apply." Pet. App. 22a; see also *id.* at 20a. Accordingly, FERC on remand ordered the parties to revise the agreement to exempt *all* "rate challenges brought by non-contracting third parties." *Devon Power LLC*, 126 F.E.R.C. ¶61,027, at 61,114 (2009). Respondents seek to revise that result, not defend it.

Respondents' theory is also fundamentally mistaken. *Mobile-Sierra* protects particular rates—those set by contract—regardless of the challenger's identity. And respondents' contention that they are "bound" to "pay certain rates" is incoherent. Five of the six respondents (two attorneys general, two end-user interest groups, and a utility regulator) do not participate in wholesale markets and are not "bound" to pay wholesale rates in any conceivable sense. None of the six (including NSTAR) is bound to pay the auction rates, because market participants can choose to contract outside the auction. And no respondent is bound to the transition rates either (which have nearly expired in any event).

Respondents alternatively argue that the auction and transition rates at issue are not "contract rates" covered by *Mobile-Sierra*. But that theory would require the Court to *expand* the relief granted below: If the rates are not contract rates, *Mobile-Sierra* would not apply of

its own force even to signatories. FERC rejected that argument below, finding that the rates at issue *are* contract rates, and the court of appeals did not address the issue. There is no reason for this Court to depart from its usual practice of declining to address matters not passed on by the court below.

In no event should the Court accept respondents' invitation to dismiss the writ as improvidently granted. Resp. Br. 16 n.1. The court of appeals decided this case on the ground that *Mobile-Sierra* is categorically inapplicable to challenges by non-parties. This Court should reverse that ruling. It can then remand, or it can address respondents' alternative arguments. But respondents cannot convert their virtual abandonment of the rationale they successfully urged on the court below into a basis for leaving the court of appeals' erroneous ruling—and its devastating consequences—in place.

I. *MOBILE-SIERRA* APPLIES TO CHALLENGES BY NON-CONTRACTING PARTIES

A. Respondents' Defense of the Court of Appeals' Rationale Is Unpersuasive

While some of respondents' *amici* defend the court of appeals' holding that *Mobile-Sierra* applies only to cases of "buyer's or seller's remorse," see, *e.g.*, CPUC Br. 7-11, respondents themselves barely offer a defense—and with reason. That holding cannot be reconciled with *Mobile-Sierra*'s foundations or with this Court's decision in *Morgan Stanley*. FERC agrees: "The court of appeals erred in holding that the *Mobile-Sierra* 'public interest' standard applies only to the contracting parties and not to third parties challenging a transaction." FERC Br. 17.

1. As respondents acknowledge (Resp. Br. 3-4), *Mobile-Sierra* rests on the sensible conclusion that rates agreed upon by sophisticated wholesale-market partici-

pants can be expected to be reasonable. That reasonableness logically cannot vary based on the identity of the person challenging the rate. See Pet. Br. 34-37. As FERC explains, the "negotiation between the[ ] parties creates the basis for presuming the contract rate to be just and reasonable," and "[w]hether a contracting party or a third party or no one at all files a complaint, the question for FERC * * * is always the same." FERC Br. 18-19. Respondents also do not deny *Mobile-Sierra*'s foundations in the necessity of contract stability. That stability would be a mirage if everyone but the contracting parties themselves could challenge contract rates unconstrained by *Mobile-Sierra*. See Pet. Br. 37-41. "If contract rates could readily be set aside at the behest of any non-contracting party, suppliers and customers would not have the assurance of stability that the *Mobile-Sierra* rule is intended to provide." FERC Br. 22.

Mobile-Sierra's public-interest standard, moreover, exists for the precise purpose of protecting the interests of non-contracting parties. See Pet. Br. 27-29. "The oddity of exempting third-party challenges from the *Mobile-Sierra* 'public interest' standard would be particularly great, given that the very point of that standard is to protect third parties." FERC Br. 19. It makes no sense to say that *the public's* right to just and reasonable rates is preserved by FERC's authority to abrogate contract rates in "extraordinary circumstances where *the public* will be severely harmed," *Morgan Stanley*, 128 S. Ct. at 2749 (emphasis added), but to exempt members of *the public* from that standard when they assert the claims themselves. The public-interest standard, moreover, is a constraint on *FERC's* authority: "Under the *Mobile-Sierra* doctrine, *the Federal Energy Regulatory Commission* * * * must presume" that contract rates are rea-

sonable. *Id.* at 2737 (emphasis added). There is no reason FERC's authority should vary depending on who initiated the proceeding before it. See Pet. Br. 29-33. On those points, respondents offer no answer.

2. Respondents likewise do not seriously dispute that the court of appeals' rationale contravenes *Morgan Stanley*. The court below held that applying *Mobile-Sierra*'s public-interest standard would "deprive [non-parties] of their statutory right to challenge rates under the 'just and reasonable' standard." Pet. App. 19a. The court thus viewed *Mobile-Sierra* as an "exception" to the statutory requirement. *Id.* at 20a. But *Morgan Stanley* flatly rejected as "obviously indefensible" the notion that "a standard different from the statutory just-and-reasonable standard applies to contract rates." 128 S. Ct. at 2740. "Rather," it explained, "the term 'public interest standard' refers to the differing *application* of that just-and-reasonable standard to contract rates." *Ibid.*

Respondents dismiss the court of appeals' error as one of "nomenclature." Resp. Br. 28-29. But that error was central to the court's decision. Because the court viewed *Mobile-Sierra*'s public-interest standard as a departure from the statutory standard, the court held that the public-interest standard could not be applied to anyone but those who had agreed, by contract, to give up their statutory rights. See Pet. Br. 24-26; Pet. App. 19a-24a. *Morgan Stanley* eviscerates the premise of that argument by making clear that the public-interest standard simply defines "what it means for a rate to satisfy the just-and-reasonable standard in the contract context." 128 S. Ct. at 2746.

Respondents nonetheless continue to insist that *Mobile-Sierra* would "deprive [them] of their statutory rights." Resp. Br. i.; see also *id.* at 22. The Federal

Power Act requires rates to be just and reasonable, but it does not grant anyone a "right" to one particular application of that just-and-reasonable standard when this Court's precedents require a different one. Under *Mobile-Sierra*, FERC must presume that rates are reasonable when set by "contract" rather than "unilaterally by tariff." *Morgan Stanley*, 128 S. Ct. at 2738-2740, 2746 n.3, 2749 n.6. That presumption rests on the nature of the rate, not the identity of the challenger. A contract rate does not cease to be a contract rate merely because it is challenged by a non-contracting party.

3. Respondents contend (at 33-36) that applying *Mobile-Sierra* to non-parties would deregulate the market in violation of *FPC* v. *Texaco Inc.*, 417 U.S. 380 (1974). But *Morgan Stanley* squarely rejected that argument:

> *Texaco* had nothing to do with [the *Mobile-Sierra*] doctrine. It held that the Commission had improperly implemented a scheme of *total deregulation* by applying no standard of review at all * * * . It did not cast doubt on the proposition that in a proper regulatory scheme, the ordinary mode for evaluating contractually set rates is to look to whether the rates seriously harm the public interest * * * .

128 S. Ct. at 2746 (citation omitted).

The fact that contracts can include *Memphis* clauses allowing parties to seek modification under the ordinary just-and-reasonable standard (Resp. Br. 24-25) does not prove that non-parties must be allowed to challenge *all* contract rates under that standard. It is far from clear that contracting parties may adopt a *Memphis* clause that applies the ordinary just-and-reasonable standard to their own challenges but not challenges by non-parties. FERC can set aside contract terms that are "unduly discriminatory," 16 U.S.C. §824e(a), and it has repeatedly

rejected discriminatory *Memphis* clauses, see, *e.g.*, *Norwalk Power, LLC*, 125 F.E.R.C. ¶61,390, at 62,839 & n.3 (2008). A blanket exception from *Mobile-Sierra* for all non-party challenges thus is hardly necessary to prevent the result that respondents disparage.

4. Respondents deny that the court of appeals' decision threatens contract stability. See Resp. Br. 40-45. But the expert federal regulator disagrees: The court of appeals' rule, it urges, would undermine "the assurance of stability that the *Mobile-Sierra* rule is intended to provide." FERC Br. 22. Respondents make light of the suggestion that "'hordes of motivated non-parties'" stand ready to challenge contract rates. See Resp. Br. 2, 32. But FERC's reports are littered with non-party challenges, including some underlying *Morgan Stanley* itself. See Pet. Br. 38-39 & nn.9-10. And the broad range of parties and *amici* before the Court today—from elected officials, to industry associations, to AARP, to the aptly named Public Citizen—makes clear that the "hordes of motivated non-parties" have arrived already.

Respondents assert that the "electric industry managed to maintain its stability and integrity for * * * five decades" despite alleged uncertainty over *Mobile-Sierra*'s scope. Resp. Br. 42-43. As millions of residents in California and elsewhere can attest, however, electricity supply has hardly been robust enough to maintain "stability and integrity." And the legal landscape was not so uncertain then as it is now. Respondents admit that, until the decision below, *no court* had rejected *Mobile-Sierra*'s applicability to non-contracting parties. See *id.* at 29. At least three court of appeals decisions, by contrast, had applied *Mobile-Sierra* to non-contracting parties. See Pet. Br. 31-32 & n.6. Respondents claim that *Northeast Utilities Service Co.* v. *FERC*, 993 F.2d 937

(1st Cir. 1993), did not address "whether a non-settling party to a settlement agreement may bring a challenge to a rate derived from that settlement agreement." Resp. Br. 30-31. While that case did not involve a challenge by a "non-*settling* party" to a "*settlement* agreement," it did involve a challenge by a non-*contracting* party to a *contract*, and the court required FERC to apply *Mobile-Sierra*. See Pet. Br. 31. Respondents' efforts to distinguish the other cases are equally unavailing.[1]

Respondents admit that *FERC* has "applied the *Mobile-Sierra* presumption to third parties" since 2002. Resp. Br. 32. While they claim FERC's practice is "far from uniform," the only contrary decisions they cite involve so-called "Reliability Must Run" agreements. See *id.* at 32-33. FERC refuses to apply *Mobile-Sierra* to that particular type of agreement only because those agreements raise special concerns. See, *e.g.*, *Bridgeport Energy, LLC*, 118 F.E.R.C. ¶61,243, at 62,193 (2007) (opining that such agreements "suppress market-clearing prices" and "deter investment in new generation"). Whether or not those concerns justify refusing to apply *Mobile-Sierra*, they are specific to that type of agreement and are not present here. Respondents, moreover, do not cite a single FERC decision holding non-party challenges exempt from *Mobile-Sierra* before 1994. And even between 1994 and 2002, FERC did apply *Mobile-Sierra* to non-parties when a court required it to do so.

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[1] Respondents urge that *Wisconsin Public Power, Inc.* v. *FERC*, 493 F.3d 239 (D.C. Cir. 2007), involved an "undue discrimination" claim. Resp. Br. 31. But the court applied *Mobile-Sierra* to reject *non-contracting parties'* claims that contracts would shift congestion costs to them. 493 F.3d at 273-275. Similarly, *Town of Norwood* v. *FERC*, 587 F.2d 1306 (D.C. Cir. 1978), stated that FERC could modify contracts as a remedy for undue discrimination *against a non-party* only if *Mobile-Sierra*'s public-interest standard was met. *Id.* at 1312.

See *Ne. Utils. Serv. Co.*, 50 F.E.R.C. ¶61,266, at 61,831-32, 61,837-39 (1990), remanded, 993 F.2d 937, on remand, 66 F.E.R.C. ¶61,332, at 62,088-92 (1994). The most that can be said for respondents' position is that FERC refused to apply *Mobile-Sierra* to non-parties for a brief period and was reversed the one time its decision was subject to judicial review.[2]

Respondents suggest that suppliers can avoid instability by settling with all those who might challenge their rates. Resp. Br. 41. The court of appeals' decision, however, exempts *all* non-contracting parties from *Mobile-Sierra*. See Pet. App. 20a, 22a. Consequently, to achieve stability, a supplier would have to settle with not only those who expressly protested the contract, but also every member of the public (currently existing or yet to be incorporated or born) that might someday be affected. Respondents never explain how that is feasible.

Finally, respondents assert that the "ordinary" just-and-reasonable standard is sufficiently protective. Resp. Br. 43-45. FERC made that same argument opposing certiorari in *Morgan Stanley* and opposing plenary review here, to no avail. See FERC Br. in Opp. in Nos. 06-1454 *et al.*, at 11-12, 17-18; FERC Pet. Br. 10-11. The argument has never been persuasive and does not improve through repetition. While cut from the same statutory

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[2] Respondents also point to the excess supply and decreasing prices in recent capacity auctions (Resp. Br. 42) but make no attempt to separate the effects of contract instability from other factors—such as the recession—that plainly affected demand. ISO-NE itself attributes the auction results to a "decline in the need for capacity and a large amount of demand resources [*i.e.*, commitments *not* to require capacity] clearing in the auction." ISO New England Inc., *Internal Market Monitoring Unit Review of the Forward Capacity Market Auction Results and Design Elements* 6 (June 5, 2009), http://www.iso-ne.com/regulatory/ferc/filings/index.html.

cloth, the ordinary just-and-reasonable standard and *Mobile-Sierra*'s public-interest standard are quite different. Respondents and the court below both describe the public-interest standard as "'much more restrictive.'" Resp. Br. 4; Pet. App. 19a. And respondents' own *amici* criticize the public-interest standard for making rates "significantly harder" to challenge. APPA Br. 31-35. Respondents cannot have it both ways: They cannot complain about the difficulty of meeting the *Mobile-Sierra* standard while pretending it is not so different from ordinary just-and-reasonable review after all.

5. Respondents' *amici* defend the court of appeals' decision in briefs that read as if *Morgan Stanley* had never been decided. CPUC, for example, devotes an entire section to arguing that "none of this Court's cases preclude[s] the Commission from modifying contract rates except in extraordinary circumstances," CPUC Br. 11-14, seemingly oblivious to *Morgan Stanley*'s square holding that "the FPA intended to reserve the Commission's contract-abrogation power for those extraordinary circumstances where the public will be severely harmed," 128 S. Ct. at 2749. CPUC's list of reasons why contract rates should *not* be presumed reasonable despite 50 years of contrary precedent largely boils down to the claim that utilities lack adequate incentives to negotiate aggressively. See CPUC Br. 21-23. Those arguments are even more unfounded today than they were 50 years ago when *Mobile* and *Sierra* were decided.[3] Respon-

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[3] States can and do take measures to ensure that utilities negotiate aggressively. Notwithstanding the filed-rate doctrine, for example, state regulators generally can "inquire into whether [a] retailer prudently chose to pay the FERC-approved wholesale rate of one source, as opposed to the lower rate of another source." *Ky. W. Va. Gas Co.* v. *Pa. Pub. Util. Comm'n*, 837 F.2d 600, 609 (3d Cir. 1988); see Economists Br. 12-13 n.7. States can also use *ex ante* mecha-

dents' *amici* disagree with *Morgan Stanley* and the half-century of jurisprudence that preceded it, but they provide no basis for overruling those precedents.

B. Respondents Are Not Distinguishable from Other Non-Parties

Respondents urge that this Court need not decide whether *Mobile-Sierra* applies to "members of the general public who are indirectly affected by wholesale energy contracts" because respondents, unlike other non-parties, are purportedly "b[ou]nd * * * to pay certain rates." Resp. Br. 20. But the court of appeals required the settlement agreement to exempt *all* non-party challenges from *Mobile-Sierra*, not just *respondents'* challenges, and FERC implemented that ruling on remand (and in scores of other cases as well). See p. 3, *supra*; Pet. Reply App. 1a-10a. Respondents' argument thus does not support the judgment they obtained. And their argument lacks merit in any event.

1. *Mobile-Sierra*'s protections attach to particular *rates*. They do not attach to particular *challengers*. *Mobile-Sierra* requires FERC to presume that rates are reasonable when set by "contract" rather than "unilater-

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nisms such as competitive bidding requirements or regulatory review of proposed contracts. See, *e.g.*, Cal. Pub. Util. Code § 454.5(b)(5), (c)(3). CPUC's suggestion that wholesale markets cannot be competitive because purchasers have an obligation to provide service (CPUC Br. 22-23) is like arguing that food markets cannot be competitive because people need to eat. And CPUC's complaints about related-party transactions (*id.* at 23) ignore FERC's authority to consider the absence of arm's-length bargaining in applying the public-interest standard. See *Ne. Utils. Serv. Co.* v. *FERC*, 55 F.3d 686, 691-692 (1st Cir. 1995). Electricity markets are far more competitive today than 50 years ago. See *Morgan Stanley*, 128 S. Ct. 2740-2742. If market imperfections were not sufficient to undermine the presumption of reasonableness then, they certainly are not now.

ally by tariff." See *Morgan Stanley*, 128 S. Ct. at 2738-2740, 2746 n.3, 2749 n.6. Each of the rationales underlying *Mobile-Sierra*'s presumption—that rates agreed upon by sophisticated buyers and sellers can be expected to be reasonable, and that contract stability is necessary for infrastructure development—rests on the nature of the rate, not the identity of the challenger. For those reasons, claims that a particular challenger is "bound" or "directly affected" are irrelevant. So long as the rate is a contract rate, *Mobile-Sierra* applies—whether the rate is challenged by an indirectly affected member of the public, a non-settling party who objected before FERC, FERC itself, or the contracting parties (the truly "bound" parties).

Of course, a claim that some entity paying a rate is "bound" to do so without its consent may bear strongly on whether it is paying a *contract* rate. A wholesale purchaser may be "bound" to pay a seller's unilaterally filed tariff rate, and *Mobile-Sierra* would not apply if the purchaser challenged that rate. But the reason *Mobile-Sierra* would not apply is that unilateral tariff rates are not contract rates, not that the purchaser's "bound" status exempts him from a *Mobile-Sierra* presumption applicable to everyone else. By contrast, where a rate is the product of an agreement—where it is a contract rate—*Mobile-Sierra* applies across the board.

2. In any event, while respondents repeatedly assert that "Respondents"—plural—are "bound" by the settlement to "pay certain rates," see Resp. Br. 8, 20, 27, five of the six respondents are not "bound" in any conceivable sense. Aside from NSTAR, respondents are the attorneys general of Connecticut and Massachusetts, the Maine Public Utilities Commission, and two end-user interest groups. See Resp. Br. ii-iii. Unless, for example,

Attorney General Blumenthal has been operating an electric utility for the benefit of his electorate in his spare time, we can safely say that none of those five entities is "bound" to pay wholesale electricity rates. An entity is not "bound" by a settlement merely because it is indirectly affected by the settlement. See *Local No. 93, Int'l Ass'n of Firefighters* v. *City of Cleveland*, 478 U.S. 501, 507-512, 528-530 (1986); Pet. Br. 41-43.

That respondents were parties to the proceedings before FERC and objected to the settlement agreement does not change their status. That proves at most that they met the broad zone-of-interests test for administrative-law standing—a test that myriad indirectly affected non-parties can satisfy. See Pet. Br. 37. If anything, respondents' participation before FERC strengthens the case for *Mobile-Sierra* protection, because respondents had a full opportunity to voice their concerns.

NSTAR likewise is not "bound" to pay the rates at issue. With respect to the auction rates, the settlement agreement's "self-supply" provision allows utilities like NSTAR to contract for capacity outside the auction or provide it themselves, thus "meet[ing] [their] capacity obligations *without paying the auction clearing price*." Pet. App. 112a (emphasis added); see Pet. Br. 10, 49. Despite the obvious relevance of that provision, respondents do not mention it even once. NSTAR is not "bound" to pay the transition rates either. See p. 26, *infra*. But even if it were, that would not justify allowing respondents to evade *Mobile-Sierra* when challenging the obligations of *other* parties that *did* agree to the rates they pay or receive under the agreement.

In any event, the claim that an entity is "bound" to pay a rate is relevant only to whether that rate is a contract rate, see pp. 16-27, *infra*, not to whether *Mobile-Sierra*

applies to non-party challenges. If NSTAR were truly "bound" to pay suppliers a particular rate, for example, that might matter if it meant NSTAR was paying a rate set unilaterally by the seller rather than a contract rate. That might make the rate NSTAR pays more susceptible to attack (by NSTAR or any other challenger). But it would not give NSTAR additional rights that other non-parties lack (much less a special right to challenge obligations that *others* voluntarily undertook). There is no reason to invent a new dichotomy between "bound" and "not bound" non-parties, or an even more vague dichotomy between "directly affected" and "indirectly affected" non-parties, when *Mobile-Sierra*'s distinction between contract rates and unilateral tariff rates already captures the relevant distinction.

3. The dangers of respondents' invitation to create a challenger-based exemption from *Mobile-Sierra* are underscored by *amici*'s proposals to exempt a variety of other categories of challengers. CPUC suggests an exception for state public utility commissions. CPUC Br. 29-33. But *Mobile-Sierra* clearly applies to proceedings that FERC initiates *sua sponte*, as *Mobile* itself makes clear. See Pet. Br. 33; FERC Br. 20-21. It makes no sense to apply *Mobile-Sierra* to the federal agency charged with superintending wholesale energy markets, but to exempt state regulators that lack FERC's expertise and congressional mandate—to say nothing of the parochial focus that makes state commissions unsuited to regulate interstate wholesale markets. CPUC claims that federal law grants state commissions "special status," CPUC Br. 30-31, but the provisions it cites concern only *procedural* rights such as intervention, see 16 U.S.C. §§ 825g(a), 825*l*. That Congress granted *only* those limited procedural rights refutes the notion that it also in-

tended state commissions to have substantively broader rights to challenge contract rates.

APPA proposes an exception from *Mobile-Sierra* for ISOs and other utilities that can pass on their costs and thus allegedly lack incentives to negotiate. APPA Br. 35-38. But that is merely a variation of CPUC's unpersuasive argument that utilities in general lack incentives to negotiate. See pp. 11-12 & n.3, *supra*. Because the same unpersuasive claims could be made about most utilities, APPA's exception would swallow the *Mobile-Sierra* rule.

This Court normally does not consider arguments raised only by *amici*. See *United Parcel Serv., Inc.* v. *Mitchell*, 451 U.S. 56, 60 n.2 (1981). Nonetheless, *amici*'s attempts to create various subcategories of exempted non-parties underscore the breadth of the ruling the court of appeals actually issued. That court held that *any* non-contracting party can challenge contract rates without regard to *Mobile-Sierra*. That result is irreconcilable with this Court's precedents, ignores *Mobile-Sierra*'s rationales, and threatens to destroy the certainty this Court sought to ensure in *Morgan Stanley* only two Terms ago.

II. The Auction And Transition Rates Are Contract Rates

There is no reason for this Court to reach out to address respondents' claim that the auction and transition rates are not contract rates. See Pet. Br. 45-46. In its order on rehearing below, FERC considered and rejected the argument that the "rates identified in the Settlement Agreement * * * are not contracts eligible for *Mobile-Sierra* protection." Pet. App. 70a-71a, 75a-76a. That issue was raised in the court of appeals only by an intervenor, see Pet. Br. 46, and that court did not address it, instead holding *Mobile-Sierra* inapplicable to particu-

lar *challengers*—*i.e.*, non-contracting parties. Indeed, *no* court has previously addressed the potentially case-specific issue of whether these auction and transition rates are contract rates. Whether *Mobile-Sierra* applies to particular challengers, and whether it applies to particular rates, are two distinct questions; this Court need not address one to address the other. And a ruling in respondents' favor on this issue would require the Court to expand the relief granted below. See pp. 3-4, *supra*; cf. *Trans World Airlines, Inc.* v. *Thurston*, 469 U.S. 111, 119 n.14 (1985). If the Court addresses the issue nonetheless, it should reject respondents' position.

A. The Auction Rates Are Contract Rates

1. The auction rates are plainly contract rates. Neither FERC nor respondents deny that the capacity auctions produce binding obligations to provide and pay for capacity, just like other contracts. See Pet. Br. 47-49. As with other contracts, those obligations are imposed only on *willing* sellers and *willing* buyers with a variety of options. See *id.* at 48-49. And conspicuously *unlike* unilateral tariff rates that ordinarily do not receive *Mobile-Sierra* protection, auction prices are not dictated by sellers; they result from an iterative bidding process in which multiple parties participate. See *id.* at 48-50.

Nor does anyone dispute that, from time immemorial, auction results have been understood to be contracts. The Uniform Commercial Code specifically addresses "sale[s] by auction" as a type of sales contract. See U.C.C. §2-328. And the leading *contracts* treatises all have sections devoted to "auctions"—sections that would not belong unless auctions produced contracts. See *Restatement (Second) of Contracts* §28 (1981); 1 R. Lord, *Williston on Contracts* §4:12, at 515-540 (4th ed. 2007); 1 J. Perillo, *Corbin on Contracts* §4.14, at 637-645 (rev. ed.

1993); see also 7 Am. Jur. 2d *Auctions and Auctioneers* §§ 49, 52, at 398, 402 (1997); 7A C.J.S. *Auctions and Auctioneers* § 53, at 642 (2004).

An auction is simply a formal, structured method of negotiating a sale price. If a buyer and seller embroiled in hard-nosed negotiation were to retain a mediator, who required them to make successive bids and offers under seal, the result would not cease to be a "contract" merely because of that element of structure. The same is true here. Far from undermining the rationales for *Mobile-Sierra* protection, moreover, the capacity auctions' structure—approved by FERC under the ordinary just-and-reasonable standard, see Pet. App. 135a-144a—reinforces those rationales because it makes prices even *more* likely to be reasonable. "[T]he real world decision makers who use the Forward [Capacity] Market do so precisely for its ability to evaluate prices." *Conn. Dep't of Pub. Util. Control* v. *FERC*, 569 F.3d 477, 484-485 (D.C. Cir. 2009) (Tatel, J.), pet. for cert. filed, No. 09-277 (Sept. 3, 2009); see also Pet. Br. 51 & n.14. And the need for contract stability is no less paramount. The auctions cannot ensure that suppliers will invest hundreds of millions of dollars in necessary infrastructure if auction prices are subject to revision years into the contract. See Pet. Br. 51-52.

While respondents repeatedly assert that auctions "bind" purchasers to pay rates against their will, that simply is not true. Because the settlement agreement's "self-supply" provision allows utilities to contract for capacity outside the auction or provide it themselves, utilities can "meet [their] capacity obligations *without paying the auction clearing price*." Pet. App. 112a (emphasis added); see Pet. Br. 10, 49. NSTAR may have objected to the *settlement*. But the auction results are separate

consensual contracts entitled to *Mobile-Sierra* protection. If ISO-NE had decided to solve New England's capacity problems by requiring its load-serving entities to negotiate contracts informally, *Mobile-Sierra* would clearly apply to the resulting contracts. There is no reason *Mobile-Sierra* would not likewise apply where, as here, ISO-NE gives load-serving entities the *choice* of either negotiating contracts outside the auction or contracting for capacity through the auction.

2. FERC's claim in its brief that the auctions do not yield contract rates is inexplicable. FERC admits that "[t]he results of the capacity auctions * * * possess[ ] certain characteristics of contracts." FERC Br. 30. It agrees that "[t]he auctions result in binding obligations by sellers to offer capacity" and "a commitment * * * to buy the amount of capacity required." *Ibid.* It concedes that auction participants can be expected to "arrive at just and reasonable rates" because auctions "share with freely negotiated contracts certain market-based features that render use of the public-interest standard appropriate." *Id.* at 36-37. And FERC's own decision below—which it now ignores—specifically rejected the argument that the "rates identified in the Settlement Agreement * * * are not contracts eligible for *Mobile-Sierra* protection." Pet. App. 70a-71a, 75a-76a.

Nonetheless, attempting once again to maximize the regulatory discretion that *Mobile-Sierra* was designed to constrain, see Pet. Br. 32-33 n.7, FERC claims that auction results are not contracts and thus should receive *Mobile-Sierra* protection only if FERC, in its beneficence, chooses to grant such protection. FERC Br. 30-31, 36-38. Respondents go further, urging that auction results are not contracts and cannot receive *Mobile-Sierra* protection even if FERC finds it necessary. Resp.

Br. 16-19, 37-40. Neither FERC's nor respondents' arguments withstand scrutiny.

Respondents urge that "the tariffs that set * * * the rules for conducting auctions are by definition not contract rates" and that "settlement provisions for * * * payments" following the auctions "were to be implemented through then yet-to-be-developed tariff revisions." Resp. Br. 16-17; cf. FERC Br. 30. That argument confuses the auction *rules* with the agreements on *rates* that result. The *rules* governing auctions, including the *rules* governing payment obligations in general terms, are set forth in the ISO's tariff. See J.A. 117-118; ISO New England Inc., FERC Electric Tariff No. 3, Market Rule 1 §§ III.13.7.2.1.1(a), III.13.7.3, http://www.iso-ne.com/regulatory/tariff/sect_3/index.html ("ISO-NE Market Rule 1"). Those *rules* can be modified under the ordinary just-and-reasonable standard. See Pet. App. 200a; J.A. 95. But the *rates* that parties agree to pay based on the auctions are *not* set forth in the tariff. They are reported to FERC in a Section 205 filing, like other contract rates. See J.A. 118; 16 U.S.C. § 824d(c); ISO New England Inc., *Forward Capacity Auction Results Filing* (Mar. 3, 2008), http://www.iso-ne.com/regulatory/ferc/filings/2008/mar/index.html. Besides, the relevant distinction is between rates set by contract and rates set "*unilaterally* by tariff." *Morgan Stanley*, 128 S. Ct. at 2738-2740, 2746 n.3, 2749 n.6 (emphasis added). Auction rates are bilateral or multilateral, not unilateral.

FERC invokes the ISO's role as the "facilitating entity at the middle of the market." FERC Br. 30. While the ISO participates as an agent,[4] that does not mean the

[4] The ISO acts as an agent on behalf of market participants. See ISO New England Inc., FERC Electric Tariff No. 3, attach. A, Market Participant Service Agreement arts. 4.1, 5.1, http://www.iso-ne.com/

auction results are not contracts; parties routinely contract through agents acting as intermediaries. See *Restatement (Second) of Contracts* § 52 cmt. c; *Restatement (Third) of Agency* § 6.01 (2006). And to the extent FERC is suggesting that the ISO is the immediate purchaser of capacity in the auctions, the auction results would still be contracts—in that case, voluntary bilateral contracts between each supplier and the ISO. See J.A. 90; *Richmond Power & Light* v. *FPC*, 481 F.2d 490, 496-497 (D.C. Cir. 1973) (*Mobile-Sierra* applies where parties "agree to a rate changeable in a specific manner"). Load-serving entities would merely be downstream purchasers who pay the ISO for the capacity they require. See p. 21 n.4, *supra*.

FERC urges that auction results are not "recorded in separate agreements between a particular generator and a particular purchasing entity." FERC Br. 30. But an auction result does not have to be "recorded" to be a contract; the contract arises from the parties' conduct—the winning participant's bid and the auctioneer's acceptance. See Pet. Br. 47-48. The very fact that treatises discuss auctions where the property is covered by the Statute of Frauds suggests there is no general requirement that auction results be "recorded." See, *e.g.*, 1 *Williston on Contracts* § 4:12, at 537-540; 7 Am. Jur. 2d *Auctions and Auctioneers* §§ 37-45, at 388-396. And each auction con-

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regulatory/tariff/attach_a/index.html; *Policy Statement on Electric Creditworthiness*, 109 F.E.R.C. ¶ 61,186, at 61,904-05 (2004). Load-serving entities remit payment to the ISO for their shares of capacity purchased in the auction, and the ISO in turn distributes payments to suppliers. See Pet. App. 112a; J.A. 70; ISO-NE Market Rule 1 §§ III.13.7.2, III.13.7.3, III.13.7.3.1; ISO New England Inc., FERC Electric Tariff No. 3, § I, Ex. ID, Billing Policy §§ 1.3, 2.4(e), (*l*), http://www.iso-ne.com/regulatory/tariff/sect_1/index.html ("ISO-NE Billing Policy").

tract *is* between a "particular generator" and either the ISO or the group of participating load-serving entities. The contract may be multilateral rather than bilateral, but it is still a contract.

FERC claims that "the consequences of default are specified not in an agreement between participants in the auction but in a tariff"—specifically, the tariff setting forth the auction rules. See FERC Br. 30-31; p. 20, *supra*. Under well-established principles, however, such auction rules are deemed incorporated into the bids made at the auction and hence into the contracts that result: "Ordinarily bidders are or should be aware of [auction] terms [that are] published or announced. A bid need not repeat such terms; it is understood as embodying them. Hence the bidder is held to the published or announced terms * * * ." *Restatement (Second) of Contracts* §28 cmt. e; see also 1 *Williston on Contracts* §4:12, at 523-525; 7 Am. Jur. 2d *Auctions and Auctioneers* §17, at 372. Besides, a contract is no less a contract merely because the consequences of default are specified elsewhere—whether in a separate agreement, another document, or background legal principles.

3. APPA argues that the auctions involve "no negotiation *at all*." APPA Br. 23-24. Not so. Suppliers compete in the auctions by offering different amounts of capacity at different prices. That process—a series of increasingly attractive offers followed by acceptance—is simply a formalized and structured form of negotiation. See p. 18, *supra*. Nor is APPA correct that there is "no privity of contract." APPA Br. 24. If the ISO is the contracting party, there is privity between each supplier and the ISO. And if the ISO is an agent, there is privity between each supplier and the group of load-serving entities that chose to acquire capacity through the auction using the ISO as

their agent. See *Restatement (Third) of Agency* §6.01(1); pp. 20-21, *supra*.[5]

That the ISO determines the installed capacity requirement administratively (APPA Br. 24-25) is also irrelevant. That is simply the total *amount* of capacity to be purchased. See Pet. App. 118a. The *price* for that capacity, and the amount (if any) each supplier will provide, are determined through the auction. The installed capacity requirement, moreover, can be challenged under the ordinary just-and-reasonable standard. See J.A. 95; *ISO New England, Inc.*, 118 F.E.R.C. ¶61,157, at 61,758 (2007).

APPA complains that the ISO can disqualify self-supply resources. APPA Br. 25. But the ISO operates an integrated transmission network in which one supplier's failure can have repercussions throughout; consequently, *all* suppliers must meet reliability qualifications. See J.A. 98-119; ISO-NE Market Rule 1 §III.13.1. The only ground for "disqualifying" a self-supply resource is failure to meet those criteria, see J.A. 65, 84, 111; cf. ISO-NE Market Rule 1 §III.13.1.6, a determination that is subject to ordinary just-and-reasonable review, see Pet. App. 119a-120a, 202a. State law might bar hospitals from hiring unlicensed physicians, for example, but that would not mean that a hospital's employment agreements with its *licensed* physicians were anything other than contracts. Likewise here, the ISO's authority to prevent

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[5] APPA also claims there is no breach-of-contract remedy. APPA Br. 24. But a supplier that did not get paid could pursue contract remedies. See *Ark. La. Gas Co. v. Hall*, 453 U.S. 571, 582 n.12 (1981); ISO-NE Billing Policy §3.4. Although the capacity auction rules sometimes specify consequences of default, see p. 22, *supra*, contracts often include such provisions, see, *e.g.*, *Restatement (Second) of Contracts* §356(1) & cmts. c-d.

load-serving entities from contracting with unreliable suppliers does not transform auction results into something other than contracts.

Finally, APPA complains about the price collar and other auction rules that limit the permissible bids and clearing prices. APPA Br. 25-26. But structured negotiations like auctions necessarily have rules. An auctioneer in a run-of-the-mill auction may specify a minimum opening bid or bid increment. It would be absurd for the winning bidder to escape his payment obligation by pointing to those limitations and claiming that his obligation is not a contract after all.

The sheer quantity of arguments that respondents, FERC, and APPA offer up should not obscure their failure to cite *any* legal authority to support them. Every leading contracts treatise—the *Restatement*, Williston, Corbin—recognizes that auction results are contracts. None suggests that particular features of these capacity auctions affect that status. This Court should not disregard longstanding, black-letter law in favor of contrived distinctions with no relevance.

B. The Transition Rates Are Contract Rates

The transition rates are also contract rates protected by *Mobile-Sierra*. While FERC admits that "the settlement represented an agreement among the signators," FERC suggests that this "agreement" is not a contract because it reflected "the resolution of a disputed proceeding before the Commission" and was "submitted to the Commission for its approval." FERC Br. 31. That argument lacks merit. That a settlement is approved by a court or agency may make it a judicial or administrative decree as well, but that character exists *in addition to* its status as a contract. See *Kokkonen* v. *Guardian Life Ins. Co. of Am.*, 511 U.S. 375, 381 (1994); *Firefighters*,

478 U.S. at 519; *Cajun Elec. Power Coop., Inc.* v. *FERC*, 924 F.2d 1132, 1135 (D.C. Cir. 1991). For that reason, "[t]he policies underlying the *Mobile-Sierra* doctrine apply with equal force to settlement agreements." *Cities of Newark* v. *FERC*, 763 F.2d 533, 546 (3d Cir. 1985) (citing *Cities of Bethany* v. *FERC*, 727 F.2d 1131, 1139 (D.C. Cir. 1984)). That FERC reviewed and approved the settlement agreement may not have been *necessary* for *Mobile-Sierra* to apply. See *Morgan Stanley*, 128 S. Ct. at 2745-2746. But it certainly did not render the agreed-upon rates any *less* likely to be just and reasonable.

FERC also urges that the transition rates apply not only to parties that signed the agreement but also to non-settling parties such as NSTAR. See FERC Br. 31. But that cannot possibly justify treating the *settling parties'* obligations as anything other than contracts. The settling parties signed the agreement specifying what each of them would pay or receive. See J.A. 163-164. Yet, under the court of appeals' holding, any non-contracting party can challenge even *those* voluntarily agreed-upon rates (not merely NSTAR's) free from *Mobile-Sierra*'s restrictions. See Pet. App. 20a, 22a. A state public official, for example, could challenge the amount a state utility had agreed to pay on the theory that the transition payments were indirectly harming consumers—even if the utility had agreed to those rates by signing the settlement. That result is impossible to square with *Mobile-Sierra*. If the transition rate *that NSTAR pays* were not a contract rate, that might mean that NSTAR (or anyone else) could challenge *what NSTAR pays* under the ordinary just-and-reasonable standard. But it could not justify stripping *Mobile-Sierra* protection from the transition rates that parties who *signed* the settlement agreed to pay or receive.

Besides, even the transition rate that NSTAR pays is a voluntary contract rate. Utilities like NSTAR can "meet their assigned [capacity] obligations through use of bilateral contracts" and thus avoid paying the transition rates. See ISO-NE Market Rule 1 §§ III.8.1, III.8.9; ISO New England Inc., *Manual for Installed Capacity (M-20)* § 2.5 (23d rev. July 1, 2009), http://www.iso-ne.com/rules_proceds/isone_mnls/index.html. And whether or not *NSTAR* agreed to the transition rates, *ISO-NE*—the entity that actually makes transition payments on behalf of load-serving entities—agreed to those rates by signing the settlement agreement. See Pet. Br. 54 n.15; J.A. 90; ISO-NE Market Rule 1 §§ III.8.1, III.8.9; *Restatement (Third) of Agency* § 6.01(1).

In any event, FERC could choose to apply *Mobile-Sierra* to a transition rate even if it were not a contract rate. Whether a rate is "just" and "reasonable" depends upon the circumstances. FERC thus has discretion to apply the statutory just-and-reasonable standard in a manner that tracks *Mobile-Sierra*'s public-interest standard when circumstances justify a similar presumption of reasonableness. See FERC Br. 22-39. Here, FERC approved the transition rates under the ordinary just-and-reasonable standard, and "[t]he short duration of the [transition] payment regime makes it unlikely that the transition payments will become unjust or unreasonable." *Id.* at 39. The widespread support for the transition rates confirms their reasonableness. If the agreement of two parties (a single buyer-seller pair) creates a presumption of reasonableness, the agreement of dozens of market participants creates a stronger presumption still. See

Pet. Br. 54 n.15.[6] The need for stability, moreover, remains acute. See *ibid.*; FERC Br. 39.

Ultimately, these complexities underscore precisely why this Court should not address the status of the transition rates. The Court ought not wade into the intricacies of whether the ISO or the load-serving entities is the contracting party, which rates are contract rates, or whether FERC has discretion to apply *Mobile-Sierra* to a rate that is not a contract rate, where no court has ever addressed those issues before. Moreover, the question is almost entirely moot. The last transition payment is due in May 2010. J.A. 164. NSTAR had a full opportunity to challenge the transition payments under the ordinary just-and-reasonable standard. See Pet. App. 120a-121a & n.32, 144a-147a. It lost on that issue before FERC, *id.* at 151a-161a, and lost again in the court of appeals, *id.* at 8a-15a. Neither NSTAR nor anyone else has filed a complaint alleging changed circumstances that might justify a different result under *any* standard. And respondents' own *amici* admit that it is unlikely such a circumstance will emerge. See APPA Br. 21-22. The Court should not expend its resources deciding a complex issue of no practical significance to the parties before it. Instead, the Court should address only the issue the court of appeals decided.

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[6] APPA downplays the support for the settlement, urging that some of the 115 parties neither signed nor opposed it. APPA Br. 15. But, as the settlement judge noted, those parties were "deemed under the regulations to have waived any objections," so that "107 parties now support the Settlement." *Devon Power LLC*, 115 F.E.R.C. ¶63,013, at 65,075 (2006) (citing 18 C.F.R. §385.602(f)(3)).

CONCLUSION

For the foregoing reasons and those set forth in petitioners' opening brief, the court of appeals' decision should be reversed.

Respectfully submitted.

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AMICUS CURIAE BRIEF

No. 08-674

IN THE

Supreme Court of the United States

NRG POWER MARKETING, LLC, *ET AL.*,
Petitioners,

v.

MAINE PUBLIC UTILITIES COMMISSION, *ET AL.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF AMICI CURIAE AMERICAN PUBLIC POWER ASSOCIATION AND NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION IN SUPPORT OF RESPONDENTS

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BRIEF OF AMICI CURIAE AMERICAN PUBLIC POWER ASSOCIATION AND NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION

INTEREST OF AMICI[1]

The American Public Power Association (APPA) represents the nation's more than 2,000 not-for-profit, publicly-owned electric utilities, which do business in every state except Hawaii. Public power systems own roughly 10 percent of the nation's electric generating capacity, and provide more than 15 percent of all kilowatt-hours of electricity sold to ultimate customers. Sixty-six New England public power systems are APPA members.

The National Rural Electric Cooperative Association (NRECA) represents the nation's 930 not-

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[1] Counsel of record for all parties received notice at least 10 days prior to this brief's due date of the amici curiae's intention to file a brief, and the parties consented to the filing. No counsel for a party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than amici curiae, its members, or its counsel made a monetary contribution to its preparation or submission.

for-profit, customer-owned rural electric cooperatives serving more than 40 million end users in 47 states. Of those 930 cooperatives, 64 are generation and transmission cooperatives that are owned by and sell power to their member distribution cooperatives. NRECA has 7 members in New England.

The members of both associations participate in wholesale power markets as buyers *and* sellers.

SUMMARY OF ARGUMENT

Contrary to Petitioners' rhetoric, this case is not about the application or scope of the *Mobile-Sierra* doctrine. [2]

In the proceeding below, ISO New England (ISO-NE) filed a tariff establishing market-wide rates, which FERC suspended and set for hearing. ISO-NE and a subset of intervenors subsequently reached a settlement purporting to set capacity rates for all market participants, whether or not they agreed to the settlement. Over the objections of some litigants, FERC approved the settlement, which included a *Mobile-Sierra* provision purporting to govern future rate challenges by *any* market

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[2] *See United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.* (*Mobile*), 350 U.S. 332 (1956); *FPC v. Sierra Pac. Power Co.* (*Sierra*), 350 U.S. 348 (1956).

participant, whether or not it signed the settlement.

Mobile-Sierra holds that freely negotiated contracts between sophisticated parties with presumptively equal bargaining power are presumed just and reasonable "as between the two [contracting parties]." *Morgan Stanley Capital Group Inc. v. Pub. Util. Dist. No. 1 of Snohomish County* (*Morgan Stanley*), 554 U.S. ___, 128 S. Ct. 2733, 2746 (2008) (internal quotation omitted). New England's capacity rates are not set through bilateral contractual arrangements to which *Mobile-Sierra* applies. Instead, these rates are set pursuant to a unilaterally-filed tariff whose terms were disputed and subsequently resolved in a Commission-approved, contested settlement.

Both Petitioners and FERC have acknowledged that the contested settlement created no initial presumption of reasonableness as to nonparties. Pet. for Writ of Cert. 7-8; FERC Br. 32-33. They concede, as they must, that FERC correctly reviewed the settlement under the ordinary just-and-reasonable standard. *E.g.*, *Mobil Oil Corp. v. FPC* (*Mobil*), 417 U.S. 283, 313-14 (1974); *Laclede Gas Co. v. FERC* (*Laclede*), 997 F.2d 936, 944 (D.C. Cir. 1993). As no *Mobile-Sierra* presumption attached to the contested settlement, the question whether the presumption would apply to third parties is not at issue.

Petitioners and FERC advance different theories as to how and why a contract-based *Mobile-Sierra* presumption could apply to ISO-NE's tariff rates, but neither holds.

FERC argues that, in approving the settlement, it had the discretion to adopt a *Mobile-Sierra* provision and make it applicable to both settlement signatories and non-signatories. This contention is flawed because, as *Morgan Stanley* explained, the *Mobile-Sierra* presumption arises from the consent of parties to contract rates, not from FERC's approval of those rates or from its determination that unilaterally-filed tariff rates are just and reasonable. Thus, the same absence of consent that precluded the application of a presumption during FERC's review of the contested settlement also bars its application to subsequent non-party challenges.

While FERC may accept contested settlements and implement disputed rates if it independently finds those rates to be reasonable, the resulting rates are tariff rates, not contract rates, at least as to the non-consenting wholesale customers.[3]

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[3] The settling parties' agreement may operate to waive their rights to seek changes to ISO-NE's tariff rates, but it does not transform those tariff rates into contract rates that FERC must presume to be reasonable as against non-consenting customers.

The application of *Mobile-Sierra* through FERC's approval of a contested settlement of a disputed, market-wide tariff would be a judicially-unprecedented and unwarranted expansion of the contract-based *Mobile-Sierra* doctrine.

Petitioners take a different and less deferential tack in defending the agency's decision. Instead of claiming that FERC had discretion to decide whether to apply *Mobile-Sierra* to New England's post-"transition period" capacity rates, Petitioners argue that FERC is required to do so because of the nature of those rates. In Petitioners' view, the incorporation of a pseudo-auction mechanism in ISO-NE's tariff-based process for setting post-transition capacity prices means that each annual rate must be considered a "contract" rate to which *Mobile-Sierra* would apply independent of the contested settlement. Pet'rs' Br. 20-21.[4] While FERC disagrees with that characterization, it nonetheless argues that the market-based features of ISO-NE's tariff rates justified FERC's exercise of discretion to presume their reasonableness. FERC Br. 36-37.

Both positions are incorrect. Although Petitioners refer to New England's post-transition ca-

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[4] Petitioners can find no similar, independent basis for applying *Mobile-Sierra* to the transition-period capacity rates established specifically by the contested settlement.

pacity rates as "auction" rates, the operation of ISO-NE's tariff rules for calculating those rates exhibits none of the hallmarks of bargaining and consent from which *Mobile-Sierra* presumptions derive. ISO-NE determines administratively the amount of capacity to be procured overall, assigning a proportional share to each load-serving entity (LSE). LSEs cannot opt out of that obligation. They may attempt to "self-supply" the required capacity, but ISO-NE may determine administratively that the proffered resources do not "qualify" to satisfy their obligations. LSEs then must pay the prices established through ISO-NE's tariff for the difference between their capacity obligations and any qualified self-supply resources.

LSEs make self-supply decisions in advance of the "auction" and have no means to establish a price above which they would prefer to self-supply capacity rather than pay ISO-NE's tariff prices. Suppliers have more flexibility to attempt to opt out of the market, but even their decisions are subject to extensive administrative controls. The "auctions" afford buyers and sellers no ability to alter the non-price terms and conditions of the products at issue and no opportunity to bargain or trade concessions. The prices resulting from this process also are subject to both a floor and ceiling established in the contested settlement.

Consequently, no *Mobile-Sierra* presumption applies here because any cause for confidence in

the reasonableness of ISO-NE's capacity rates derives from faith in the reasonableness of the applicable tariff rules, not the "consent" of buyers and sellers. Phrased differently, if merely purchasing service under tariff rates were sufficient to support a *Mobile-Sierra* presumption, then *all* rates—whether established by contract or tariff—would be subject to such presumptions. Neither this Court nor any other has suggested that result. On the contrary, *Morgan Stanley* itself—and the distinction it drew between tariffs and contract rates—renders such a result untenable.

Petitioners ask the Court to avoid addressing whether New England's capacity rates are contract rates to which *Mobile-Sierra* applies. Instead, they urge consideration of a question not presented: how the *Mobile-Sierra* doctrine, *once triggered*, applies to various third parties. Petitioners point to the purported evils of permitting indirectly-affected third parties to challenge bilateral power sales agreements free of the *Mobile-Sierra* presumption that applies to the contracting parties themselves. But such concerns are not at issue in this case, and the Court should reject this gambit.

If the Court nonetheless addresses this issue, it should tread cautiously, recognizing the widely varied circumstances in which parties sign contracts. Contracts through which independent system operators, such as ISO-NE, procure services

from generators and transmission owners are of particular concern. Independent system operators like ISO-NE are non-profit corporations without any shareholders and are virtually guaranteed to recover whatever costs they incur from ratepayers. In such circumstances, APPA and NRECA submit, FERC may not simply presume that the rates that such entities agree to incur and pass on will be reasonable.

Finally, the Court should reject Petitioners' remaining arguments. The decision below does not violate *Morgan Stanley*'s holding that the just-and-reasonable standard is the only statutory standard for reviewing public utility rates. Nor would application of the public-interest version of the just-and-reasonable standard adequately protect dissenting wholesale customers just because those customers are "members of the public." Pet'rs' Br. 24. Petitioners well understand that the *Mobile-Sierra* public-interest test not only protects different interests than ordinary just-and-reasonable review, but also typically requires a materially greater showing of harm to those interests to justify rate changes. That the public-interest test is "much more restrictive" than the ordinary just-and-reasonable standard is exactly why Petitioners seek to impose it on both contracting and non-contracting parties.

This case should be easily decided. Respecting freedom of contract means honoring dissenting customers' *refusals* to contract on par with the set-

tling parties' decisions to contract. Even if FERC accepts tariff rates upon making an independent finding that they are reasonable, subsequent requests for rate changes—at least by the non-consenting wholesale customers—must be subject to ordinary just-and-reasonable review.

ARGUMENT

I. AS FERC CONCEDES, NEW ENGLAND'S CAPACITY RATES ARE TARIFF RATES TO WHICH *MOBILE-SIERRA* DOES NOT APPLY.

Petitioners' arguments notwithstanding, this is not a *Mobile-Sierra* case. Petitioners argue that the Court need not address whether New England's capacity rates are contract rates, urging that the question be left to the D.C. Circuit in the first instance. That puts the cart before the horse. If New England's capacity rates are not contract rates, as we demonstrate below and as FERC concedes,[5] then *Mobile-Sierra* is inapplicable and the question of whether or how it applies to third parties does not arise. As the Court generally does not decide unnecessary questions, *e.g.*, *Conn. Dep't of Pub. Safety v. Doe*, 538 U.S. 1, 7 (2003), it should not

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[5] FERC Br. 30.

reach Petitioners' arguments about restrictions upon third parties.[6]

A. *As this Court, Petitioners, and their amici have recognized,* Mobile-Sierra *applies only to contract rates, not tariff rates imposed on unwilling customers.*

From *Mobile* to *Morgan Stanley*, this Court has not wavered in distinguishing contract rates from tariff rates. Contract rates establish the rates to be charged "to particular customers" who agree to them. *Mobile*, 350 U.S. at 338. Tariff rates are rates of general applicability established without customer consent. The distinction is crucial for *Mobile-Sierra* purposes. As Petitioners themselves acknowledge, "this Court has repeatedly grounded

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[6] In any case, as explained in Section III below, the answer to Petitioners' question—whether *Mobile-Sierra* applies to third parties—should be "it depends." Whether FERC must presume a contract to be reasonable under *Mobile-Sierra* depends on whom the contract affects, how directly, and whether the directly-affected parties agreed to the rates, rejected them, or were absent from the negotiations. If a categorical answer is required, the answer must be that where, as here, parties directly and substantially affected by a contract were not present at its negotiation or refused to sign it, FERC may not presume that contract to be reasonable in the context of challenges brought by non-signatories.

Mobile-Sierra in the sensible notion that a rate agreed upon by a buyer and seller—*as opposed to a tariff dictated unilaterally by the seller*—can be expected to be reasonable." Br. 34 (emphasis added). In contrast, "[t]he *Mobile-Sierra* doctrine does not apply when rates offered to prospective customers are established unilaterally through *ex parte* filings." Elec. Power Supply Ass'n Br. 22 (citing *Morgan Stanley*, 128 S. Ct. at 2746 n.3).[7]

The decision below[8] is consistent with *Mobile-Sierra's* contractual foundations, while Petitioners' view conflicts with them. The Federal Power Act (FPA), 16 U.S.C. §§ 791a-825r, "'departed from the scheme of purely tariff-based regulation and acknowledged that contracts between commercial buyers and sellers could be used in ratesetting.'" *Morgan Stanley*, 128 S. Ct. at 2738 (quoting *Verizon Commc'ns Inc. v. FCC* (*Verizon*), 535 U.S. 467, 479 (2002)). The FPA thus permits utilities to set rates "with individual electricity purchasers" through bilateral contracts, *id.* at 2738 (citation omitted), and, when they do so, *Mobile-Sierra* requires FERC to presume that "the rate[s]

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[7] *See also* Morgan Stanley Capital Group Br. 5 ("The degree of latitude possessed by FERC to modify an existing rate . . . varies depending on whether the rate was established unilaterally by tariff or instead by a negotiated contract.").

[8] *Me. Pub. Utils. Comm'n v. FERC* (*Maine Public*), 520 F.3d 464 (D.C. Cir. 2008).

set out in [such] freely negotiated wholesale-energy contract[s] meet[] the 'just and reasonable' requirement ...." *Id.* at 2737.

But while sophisticated buyers and sellers can look out for their own interests and trade other benefits in exchange for rights to mount later challenges—giving rise to a presumption that the resulting agreement is reasonable "'as between the two of them,'" 128 S. Ct. at 2746 (quoting *Verizon*, 535 U.S. at 479)—their agreement establishes no presumption as to other entities. *See Verizon*, 535 U.S. at 479 ("[T]he principal regulatory responsibility [is] not to relieve *a contracting party* of an unreasonable rate ....") (citing *Sierra*, 350 U.S. at 355) (emphasis added).

Petitioners praise the Court's "'commonsense notion that "[i]n wholesale markets, the party charging the rate and the party charged [are] often sophisticated businesses enjoying presumptively equal bargaining power, who could be expected to negotiate a 'just and reasonable' rate *as between the two of them*."'" Pet'rs' Br. 7 (quoting *Morgan Stanley*, 128 S. Ct. at 2746, and *Verizon*, 535 U.S. at 479) (emphasis added). However, Petitioners acknowledge that the expectation's *limits* are "why [*Mobile-Sierra*] applies to rates 'set bilaterally by contract' but not those set 'unilaterally by tariff.'" *Id.* at 23 (citing *Morgan Stanley*, 128 S. Ct. at 2738).

For these reasons, the fate of Petitioners' challenge hinges on whether ISO-NE's capacity rates are contract rates, not tariff rates. Their position that ISO-NE's capacity rates are contract rates depends in turn on viewing *some* parties' agreement to the settlement as sufficient to require FERC to treat the settlement and the resulting rates as presumptively-reasonable contract rates with respect to *all* of the customers who will pay them. *Cf.* Pet'rs' Br. 19, 35 ("[C]ontract rates negotiated by sophisticated parties can be expected to be reasonable even insofar as they affect third parties.").

Amici Colin C. Blaydon *et al.* (collectively, "Economists") assert that wholesale contracts that are "presumptively reasonable as between the parties because of the 'superior efficiency of private bargaining'" must also be deemed "presumptively reasonable as to third parties." Econ. Br. 9-10 (quoting Pet'rs' App. 19a). In their view, "[c]ontract law and economic theories of contract rest on the common understanding that, because of the efficiency of private bargaining, buyers and sellers are able to negotiate contracts that maximize gains not only for themselves but also for society as a whole." *Id.* (quoting Pet'rs' App. 22a). But the *reason* why private bargaining purportedly produces gains for "society as a whole" is that buyers and sellers negotiate prices based on the unique value each ascribes to the relevant goods or services, and each receives

something they value more highly than what they give. In contrast, forcing unwilling purchasers to buy prescribed amounts of a product at prices they consider to be excessive is not an efficient market outcome. Nor is it rendered efficient by the fact that *other* purchasers deemed the prices reasonable.

Elsewhere, the Economists seem to admit as much, noting that *Mobile-Sierra* "is premised on the agreement of willing and sophisticated parties," *id.* at 14, and "would not be interpreted to permit one party to 'thrust' unilaterally upon others terms to which they 'have vociferously objected.'" *Id.* at 14-15 (quoting Pet'rs' App. 22a). But that is exactly what happened here. In fact, the Economists do not appear to criticize the D.C. Circuit for its resolution of the case before it, involving a "cram-down[] ... where agreement is only reached by a subset of the negotiating parties." *Id.* 15 n.8. They merely object that "[t]he D.C. Circuit made no effort to confine its holding to the situation before it." *Id.* at 19.

FERC and Petitioners seek to paint a different picture of the facts by focusing on what appears, superficially, to be overwhelming support for the contested settlement with only a few objectors.[9]

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[9] The Commission states (Br. 7) that of "the 115 parties participating in the settlement proceedings, only eight parties

Assuming a headcount were relevant, however, the truth is otherwise. Of the 115 votes cast on the proposed settlement, only 61 supported it. Another 46 were cast by parties who remained neutral, neither opposing settlement approval nor signing the agreement, and 8 votes formally opposed the settlement. Moreover, of the 61 "signatory votes," 22 were cast by 6 groups of affiliated entities, including 5 votes cast by Petitioners.[10]

As these data reveal, although only one load-serving entity actively opposed it, misgivings about the settlement were far more widespread. And the one distribution company that formally opposed the settlement, Respondent NSTAR Corporation, serves much of the Boston, MA metropolitan area and accounts for approximately 25 percent of New England's electrical load.[11] The decision by sophis-

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formally opposed the agreement." Petitioners go further, reciting the same math (Pet'rs' Br. 9), and observing that "[i]f the agreement of *two* parties (a single buyer-seller pair) creates a presumption of reasonableness, the agreement of *dozens* of buyers and sellers creates a stronger presumption still." *Id.* at 53 & n.15.

[10] Attach. A to Reply Comments of New England Power Pool Participants Committee in Support of Settlement Agreement, Docket No. ER03-563 (Sept. 5, 2006), *available at* FERC eLibrary Accession no. 20060405-5083 (http://elibrary.ferc.gov/IDMWS/common/opennat.asp?fileID=10992290).

[11] Respondents' Br. 8, 20.

ticated parties *not* to join the settlement undercuts any attempt to extrapolate a general presumption of reasonableness from other parties' decisions to settle.

No decision of this Court or any lower Court of Appeals suggests that rates to all wholesale customers may be established (and subjected to a reasonableness presumption) by contract between only some buyers and sellers. On the contrary, decisions of this Court and lower courts expressly hold otherwise. In 1974, this Court established the "correct legal principles," *Mobil*, 417 U.S. at 313, governing the Commission's assessment of "settlement proposal[s] that lack[] unanimous agreement ...." *Id.* at 312. That some parties agreed to the deal "did not, of course, establish without more the justness and reasonableness of its terms." *Id.* at 312-13. Instead, the Court explained:

> If a proposal enjoys unanimous support from all of the immediate parties, it could certainly be adopted as a settlement agreement if approved in the general interest of the public. But even if there is a lack of unanimity, it may be adopted as a resolution *on the merits*, if FPC makes an independent finding supported by "substantial evidence on the record as a

> whole" that the proposal will establish "just and reasonable" rates ....

Id. at 314 (quoting *Placid Oil Co. v. FPC*, 483 F.2d 880, 893 (5th Cir. 1973), *aff'd*, *Mobil*) (underlined emphasis added).

Thus, the Court affirmed the Fifth Circuit's inquiry into "whether, viewing the terms of the proposal not as a traditional settlement but as a result of an administrative decision, it falls within that 'zone of reasonableness' which is supported by 'substantial evidence on the record as a whole.'" *Placid Oil*, 483 F.2d at 894. Numerous D.C. Circuit cases are in accord.[12]

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[12] *E.g.*, *Kelley ex rel. Mich. Dep't of Natural Res. v. FERC*, 96 F.3d 1482, 1489-90 (D.C. Cir. 1996) ("[A] settlement that is forced onto a party is effectively converted into a decision 'on the merits'" (citing *Mobil*, 417 U.S. at 314)); *Laclede*, 997 F.2d at 946 ("reject[ing] the notion that any settlement, solely because of its status as such, is reasonable" (citing *Tejas Power Corp. v. FERC*, 908 F. 2d 998, 1003 (D.C. Cir. 1990))); *Tejas Power Corp.*, 908 at 1003-04; *Consol. Gas Supply Corp. v. FERC*, 606 F.2d 323, 330 (D.C. Cir. 1979) ("The standard for judicial review of [a FERC order on] a contested settlement proposal is ... whether the Commission has made an independent rate determination supported by substantial evidence ... "), *cert. denied*, 444 U.S. 1073 (1980). In making its independent determination, FERC may accord "some weight" to the number of customers supporting or not opposing the agreement, but a headcount is not dispositive. *Laclede*, 997

Contested settlements create no presumption of reasonableness because the element essential to that presumption—consent of the directly-affected parties—is missing. Because that consent is missing, FERC must make an "independent finding ... that the proposal will establish 'just and reasonable' rates," *Mobil*, 417 U.S. at 314 (internal quotation omitted). FERC is therefore correct to concede that "the rates covered by the settlement's public-interest review provision are not themselves contract rates to which the Commission was required to apply *Mobile-Sierra*." FERC Br. 15 (emphasis omitted).

B. The use of Memphis *clauses illustrates why non-contracting customers face no* Mobile-Sierra *presumptions.*

The role of *Memphis*[13] clauses in *Mobile-Sierra* jurisprudence further illustrates the absurdity of Petitioners' position that contested settlements entered into by some wholesale customers

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F.2d at 946.

[13] *United Gas Pipe Line Co. v. Memphis Light, Gas & Water Div.* (*Memphis*), 358 U.S. 103 (1958); *see also Morgan Stanley*, 128 S. Ct. at 2739.

can establish *Mobile-Sierra* presumptions running against all wholesale customers.

As the Court has explained, *Mobile-Sierra* is a restriction on the use of the FPA's rate-change procedures to evade or to void valid contract obligations, unless the public interest requires it. As stated in *Mobile*, "[a]bsent the Act, a unilateral announcement of a change to a contract would ...be a nullity," and nothing in the Act affected that result. 350 U.S. at 339. *Sierra* reached a similar conclusion, holding that FERC could relieve a contracting party of its valid contract obligations only when the public interest so required. *Sierra*, 350 U.S. at 355. Yet contracting parties may preserve their rights to make rate changes under FPA Section 205, 16 U.S.C. § 824d, or to seek changes under FPA Section 206, 16 U.S.C. § 824e, by including such rights expressly in so-called *Memphis* clauses.

Such savings clauses are needed, however, only to preserve rights that the contracting parties otherwise would be deemed to bargain away by entering into the contract. Where an entity has not bargained away any rights, there is neither a need nor an opportunity for it to negotiate any savings clause.

This structure puts the lie to Petitioners' claims that *Mobile-Sierra* "applies" to non-contracting parties and that it precludes application of the ordinary just-and-reasonable standard

when non-settling parties challenge rates imposed upon them by a contested settlement and subsequent tariff filing. It makes no sense to say that settling parties may avoid the *Mobile-Sierra* presumption by negotiating a savings clause preserving their right to seek changes under an ordinary just-and-reasonable standard, but non-settling parties—who never agreed to the deal in the first place and never bargained away any rights—must satisfy the "much more restrictive" (Pet'rs' App. 19a (internal citations omitted)) public-interest test.

C. *The transition-period capacity rates are tariff rates to which* Mobile-Sierra *does not apply.*

The contested settlement establishing New England's capacity market set forth specific, dollars-per-kilowatt-month capacity rates to be charged during the so-called "transition period," which began in December 2006 and runs until mid-2010. Pet'rs' App. 116a. Under *Mobil*, there can be no credible argument that a *Mobile-Sierra* presumption attaches to tariff rates adopted under a contested settlement. As FERC aptly observes:

> The transition payments apply to all suppliers and purchasers of capacity—including the contesting parties and all future entrants into the market—not just to the settling parties.

> *As to these other participants, the transition payments do not resemble contractually negotiated rates at all.*

FERC Br. 31 (emphasis added).[14]

Petitioners advance no serious argument to the contrary. Petitioners assert that "the transition-payment obligations *of the settling parties* are clearly 'contract rates' entitled to *Mobile-Sierra* protection," Pet'rs' Br. 53, but that is not the issue. On the real question, "[w]hether transition-payment obligations imposed on non-signatories would be contract or unilateral tariff rates, and whether FERC could impose *Mobile-Sierra* protection even in the latter event," *id.* at 53-54 n.15, Petitioners claim that the matter is "complex" and repeat their entreaty that the Court refrain from passing on it.

Other than a passing reference to its "interest in the stability of the settlement," FERC Br. 39, the agency never explains how or why FERC reasonably could apply a *Mobile-Sierra* presumption to what are unquestionably tariff rates. FERC and Petitioners' focus on the short time during which

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[14] *See also id.* 16 ("The rates at issue here are set not by private contract, but pursuant to a tariff that was contained in a contested settlement ... ," and "[t]he Commission therefore was not required to prescribe the public-interest standard for future challenges to [those] rates ....").

the transition rates would be in effect (*id.*; Pet'rs' Br. 52) does not justify application of an otherwise-inapplicable *Mobile-Sierra* presumption; on the contrary, the limited time remaining demonstrates that it is unlikely that a challenge could be filed, let alone succeed, under an *ordinary* just-and-reasonable standard based on changed circumstances. In any event, for the reasons explained below, FERC lacks discretion to create or adopt a *Mobile-Sierra* presumption where the contracting parties' agreement is insufficient to do so by itself.

D. ISO-NE's post-transition capacity rates are tariff rates to which Mobile-Sierra *cannot apply.*

FERC and Petitioners take somewhat different tacks with respect to ISO-NE's post-transition, tariff-based capacity rates. Petitioners claim (Br. 47) that each payment of a tariff rate that uses an auction mechanism to establish the price is a separate contract to which *Mobile-Sierra* will apply regardless of whether the contested settlement (or FERC's approval of it) could effectuate that result. FERC disagrees, finding that the so-called auctions "will not result in contracts between buyers and sellers," but arguing nonetheless that "they share with freely negotiated contracts certain market-based features that render use of the public-interest standard appropriate." FERC Br. 36. Both arguments are incorrect. ISO-NE's post-transition

capacity rates are not contracts and lack the qualities necessary for FERC to presume their reasonableness—either initially or in light of changed circumstances.

1. ISO-NE's post-transition capacity rates are not contract rates.

Petitioners argue that because ISO-NE's method for determining post-transition capacity rates includes certain elements of an auction, the resulting rates are contract rates. Petitioners are incorrect. Tellingly, despite their insistence that auctions produce contracts, Petitioners do not seem certain with whom they will be contracting. *Compare* Pet'rs' Br. 49 ("Those that choose to acquire capacity through the auction ... are responsible for paying for capacity at the auction price ... [and], therefore, the auction rates reflect voluntary agreements between buyers and sellers.") *with id.* at 48 ("Before each auction, ISO-NE determines the amount of capacity *it* will purchase—the 'installed capacity requirement'—according to processes it develops in consultation with utilities and other stakeholders.") (emphasis added).

In fact, ISO-NE's method for determining post-transition period capacity rates includes few, if any, of the hallmarks of freely negotiated contracts among sophisticated parties from which the *Mobile-Sierra* presumption derives. Indeed, there is no

negotiation *at all* and no privity of contract between the sellers supplying the capacity and the wholesale customers paying the resulting rates. Neither buyers nor sellers have a breach of contract remedy against the other in cases of default.[15] Most important, the exercise of parties' independent business judgment is largely supplanted or constrained by the operation of ISO-NE's tariff rules.

On the demand side, ISO-NE dictates administratively both the overall amount of capacity that must be procured in order to maintain reliability and the portion of that total amount for which individual customers must pay. *See* Pet'rs' App. 85a. ISO-NE's calculation of the total "Installed Capacity Requirement" (ICR) depends on both its administrative determination of the level of reliability to be achieved and its assumptions about the types of capacity available, their dependability, and the amount of capacity that will be necessary to achieve its selected reliability standard. *See ISO New England Inc.*, 127 F.E.R.C. ¶ 61,142, PP 3-9 & n.5 (2009). The magnitude of the administratively-determined ICR—*i.e.*, the amount of capacity that must be procured—directly affects the capacity rates that ISO-NE charges LSEs under its tariff.

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[15] *Compare* Pet'rs' Br. 48 ("[W]here winning bidder fails to pay, 'the seller is justified in treating the contract as breached or rescinded'" (quoting 7A C.J.S. *Auctions and Auctioneers* § 53, at 642 (2004)).

Conn. Dep't of Pub. Util. Control v. FERC, 569 F.3d 477, 478-79 (D.C. Cir. 2009) (ICR is "a key input into the market-based mechanism that determines transmission tariffs and end-user costs in the New England bulk power system"), *petition for cert. filed*, No. 09-277 (U.S. Sept. 3, 2009); Pet'rs' App. 26a.

While customers may "self-supply" capacity in lieu of paying ISO-NE's capacity rates, they may not choose to purchase or self-supply less than the ISO requires. Their ability to "self-supply" also is constrained, in that the ISO determines administratively whether and to what extent self-supplied resources "qualify" to supplant the obligation to pay ISO-NE's rates. Pet'rs' App. 112a-113a. ISO-NE's "auction" offers no mechanism to negotiate bilaterally either reduced requirements, less stringent qualification criteria, or changes in non-price terms. In short, contracting freedom on the demand side of ISO-NE's capacity "auctions" is dramatically constrained.

Similarly, on the supply side, ISO-NE rules dictate the characteristics that resources must exhibit in order to qualify as "capacity resources" under its tariff.[16] They also limit both the bids that

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[16] In other words, ISO-NE's resource-qualification requirements constrain customers' flexibility to choose to pay lower capacity rates in exchange for less reliable capacity resources.

sellers may submit, specifying the prices below which they no longer are willing to sell into the market, and their ability actually to leave the market if prices drop below that level but their resources are needed for reliability.

The resulting "market" prices are further constrained by a "price collar," *i.e.*, by floor and ceiling prices equal to 0.6 times and 1.4 times the "Cost of New Entry" calculated in accordance with the settlement. Joint App. 132. The contested settlement provides for that price collar to remain in place "[f]or the lesser of five FCAs or three Successful FCAs." *Id.*

In these circumstances, there is no basis for a *Mobile-Sierra* presumption. Any confidence in the reasonableness of New England's capacity prices derives from faith in the tariff rules that produce those rates, not from the "consent" of the buyers and sellers paying or being paid those rates. If taking and paying for tariff-required service was sufficient to support a *Mobile-Sierra* presumption, then *all* rates—whether established by contract or tariff—would be subject to such presumptions. *Morgan Stanley* reaches precisely the opposite result.

2. Because *Mobile-Sierra* is contract-based and ISO-NE's capacity rates are tariff-based, FERC lacked "discretion" to apply *Mobile-Sierra*.

FERC correctly concludes that ISO-NE's post-transition capacity rates are not contract rates to which the Act required it to apply a *Mobile-Sierra* presumption. It errs, however, in assuming that FERC had the "discretion" to apply a contract-based, *Mobile-Sierra* presumption to non-contract rates. FERC had no discretion to treat an apple as if it were an orange. For the same reason that FERC is not permitted to presume the reasonableness of tariff rates initially, it may not adopt a presumption that they will remain reasonable despite changed circumstances. FERC's contrary position fails to appreciate the reasons behind the *Mobile-Sierra* presumption and *Morgan Stanley*'s emphasis on the differences between contract rates and tariff rates. It also distorts the statutory scheme and impermissibly impairs FERC's own regulatory authority.

Over the dissenting opinion of two Justices, *Morgan Stanley* drew a distinction between tariff rates and contract rates, *e.g.*, 128 S. Ct. 2749 n.6, and required FERC to presume the reasonableness of freely-negotiated, fixed-price contracts unless the public interest demanded otherwise. *Morgan*

Stanley further required FERC to apply that presumption regardless of whether it had any prior opportunity to review the contract rates. The Court explained that the *Mobile-Sierra* presumption arises from the parties' consent to contract rates, not from FERC's acceptance of them. *See id.* at 2746. Moreover, the reason why *Mobile-Sierra* presumptions last for the duration of contract rates, even in the face of changed circumstances, is that freely-negotiated, fixed-price contracts inherently allocate the risks of changed circumstances, and those allocations are presumptively reasonable as well. *See N. Ind. Pub. Serv. Co. v. Carbon County Coal Co.*, 799 F.2d 265, 278 (7th Cir. 1986) ("[A] fixed-price contract is an explicit assignment of the risk of market price [changes]"); Econ. Br. 17 ("[C]ontracting parties have allocated the risk of price fluctuations *between themselves*") (emphasis added).

FERC's position that it had "discretion" to apply a *Mobile-Sierra* presumption to tariff rates ignores these premises and the fundamental differences between tariff and contract rates. Unlike fixed-price contracts, tariff rates include no presumptively-reasonable allocation of future risks. Nor can FERC's acceptance of a tariff rate create such an ongoing reasonableness presumption, for several reasons. First, *Morgan Stanley* holds that *Mobile-Sierra* presumptions arise from parties' consent, not from FERC's regulatory judgment that a

rate is just and reasonable. If an absence of consent precludes the presumption from attaching initially, FERC's acceptance of the rate cannot supply it. To hold otherwise would be to treat *Mobile-Sierra*, contrary to *Morgan Stanley's* teaching, 128 S. Ct. at 2746, as an estoppel doctrine preventing FERC from revisiting the reasonableness of rates it initially accepted.

The conclusion that FERC lacks "discretion" to apply a *Mobile-Sierra* presumption to tariff rates also flows from the nature of the doctrine as a limitation of FERC's authority. *See* Pet'rs' Br. 27 ("*Mobile-Sierra* limits *FERC's authority* to abrogate contract rates."). While regulatory agencies may choose not to *exercise* their authority—assuming that such restraint is consistent with the obligations that Congress has placed upon them—agencies cannot *limit* their authority. Only Congress may do that. In accepting the tariff setting forth ISO-NE's capacity rates, FERC could legitimately emphasize the need for rate stability and could even announce its intention to look with disfavor upon requests for rate changes, but FERC's current policy views and its initial assessment of ISO-NE's tariff rates carry no greater weight than the views that FERC might subsequently bring to a later assessment of those rates in light of changed circumstances.[17] FERC cannot apply a *Mobile-*

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[17] In performing such a later review, the FPA still would re-

Sierra presumption to ISO-NE's tariff-based capacity rates because of the absence of a freely-negotiated, fixed-price contract invoking that presumption and limiting FERC's authority.

FERC's attempts to justify its purported discretion to adopt a *Mobile-Sierra* presumption are unpersuasive. FERC first poses a faulty analogy between capacity rates calculated in accordance with ISO-NE's tariff and rates contained in power-sales agreements freely negotiated by buyers and sellers under market-based rate tariffs. FERC Br. 36-37. But for the reasons set forth above, *see supra* pp. 24-27, ISO-NE's tariff-based mechanism for calculating capacity rates has little in common with freely-negotiated, bilateral power sales agreements. That FERC may rely on freely negotiated contracts among buyers and sellers without market power to establish just and reasonable rates does not mean that capacity priced under the tariff-based mechanisms of a central market administrator also can be presumed just and reasonable.

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quire FERC to balance consumer and investor interests and therefore to give due weight to investments that may be made in reasonable reliance upon an expectation of rate continuity. But the precise balance to be struck is a matter for that later Commission to decide.

Second, FERC argues (Br. 38) that "application of the public-interest standard to auction results would promote an important interest in rate stability." But FERC itself seems to acknowledge that its "interest in rate stability," however important, cannot enable the agency to create a *Mobile-Sierra* presumption absent parties' consent to contract rates. FERC therefore "couple[s]" its finding regarding the need for rate stability with "the presumptively just and reasonable nature of the auction prices." *Id.* But that is circular reasoning. The very thing that FERC sought to prove was *whether* it was permitted to presume the reasonableness of ISO-NE's post-transition capacity rates.

II. THE PUBLIC-INTEREST TEST DOES NOT ADEQUATELY PROTECT NON-CONSENTING WHOLESALE CUSTOMERS

Petitioners attempt to downplay the impact of imposing the "'much more restrictive'" (Pet'rs' App. 19a (internal citations omitted)) public-interest standard on rate challenges by non-consenting wholesale customers, suggesting that such customers are "members of the public" whom FERC may protect under that standard. *E.g.*, Pet'rs' Br. 19, 28 ("[T]he relevant harm [under *Mobile-Sierra's* public-interest test] has always been harm *to the public*, *i.e.*, to third parties."). Petitioners' argument is premised on semantics, not

substance. Petitioners know full well that applying *Mobile-Sierra*'s public-interest standard would make it significantly harder for dissenting wholesale customers to challenge the rates imposed on them. If *Mobile-Sierra's* applicability or inapplicability made no difference, they would not have brought this case before the Court.

The mere fact that dissenting wholesale customers are members of the public does not mean they will receive the same protection under *Mobile-Sierra*'s public-interest test as they would under ordinary just-and-reasonable review. Contracting parties are "members of the public" too, but no one argues that the public-interest test protects them to the same extent or in the same way as would have been the case if they had preserved their rate-change rights through a *Memphis* clause. While FERC and the courts have applied *Mobile-Sierra*'s public-interest test with varying degrees of stringency,[18] the most common formulations suggest

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[18] In some cases, courts have found the public-interest test satisfied simply by a FERC finding that non-parties (as opposed to the contracting parties themselves) may be harmed by the parties' contracts. *Ne. Utils. Serv. Co. v. FERC*, 55 F.3d 686, 692 (1st Cir. 1995). In other cases, courts have construed the public-interest test as "practically insurmountable," *Papago Tribal Util. Auth. v. FERC*, 723 F.2d 950, 954 (D.C. Cir. 1983), *cert. denied*, 467 U.S. 1241 (1984), justifying rate changes only in "extraordinary circumstances," *Ark. La. Gas Co. v. Hall*, 453 U.S. 571, 582 (1981), of "unequivocal

that applying the public-interest standard changes not only the identity of the entities whose harm may be considered but, also, the magnitude of the harm that must be demonstrated to justify a rate challenge.

Mobile-Sierra's distinction between private interests and the public interest arose in cases where the only wholesale customers paying the contract rates were the parties to the contract. In such cases, limiting rate changes to situations where the public interest requires it is just another way of saying that the FPA does not relieve contracting parties of their improvident bargains. And where contracting parties advance public-interest claims that happen to align with their private interests, it makes sense to treat those claims skeptically and to require convincing proof that the public interest would be harmed substantially by continuation of the agreed-upon rates.[19]

Wholesale customers attempting to challenge rates imposed on them without their consent stand

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public necessity," *Permian Basin Area Rate Cases*, 390 U.S. 747, 822 (1968) (citing *Mobile*).

[19] *See Potomac Elec. Power Co. v. FERC*, 210 F.3d 403, 406 (D.C. Cir. 2000), in which a panel that included two judges later to hear the case below affirmed FERC's rejection of contract-modification claims by a party, including those dressed up as requests for *sua sponte* action to protect third parties.

on different footing, however. They are not merely "members of the public" whom FERC must protect as part of the general public interest. They are the immediate customers paying rates subject to the Commission's jurisdiction. Their interests in the reasonableness of jurisdictional wholesale rates are neither attenuated nor indirect. The FPA requires FERC to ensure that jurisdictional rates in all wholesale transactions are just and reasonable. Private agreements between public utilities and *some* customers cannot affect the mode of analysis that FERC applies in determining whether that commandment has been satisfied with respect to other customers.

If there had been no contested settlement in this case and FERC had simply accepted a unilateral ISO-NE tariff filing, no one could dispute that any wholesale customer subject to the tariff rates could seek rate changes later based on changed circumstances. Nor could anyone dispute that FERC would review such requests under an ordinary just-and-reasonable standard. Here, ISO-NE's capacity rates are the result of a tariff filing made to implement a contested settlement, which FERC found to be just and reasonable despite Respondents' objections. From the perspective of a wholesale customer who did not sign the settlement, these facts are no different from the hypothetical above. Yet Petitioners in this case would prevent FERC from modifying the rates that such customers pay unless

they can show that failure to do so would "severely harm[]" the public interest, *Morgan Stanley*, 128 S. Ct. at 2749. There is no basis for that judicially-unprecedented result.[20]

III. WHETHER AND HOW *MOBILE-SIERRA* SHOULD APPLY TO "INDIRECTLY-AFFECTED" THIRD PARTIES DEPENDS ON THE FACTS.

We have contended that where, as here, some wholesale customers agree to a tariff rate and others oppose it, FERC may accept those rates if it independently finds them to be just and reasonable but that no *Mobile-Sierra* presumption attaches to

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[20] We say "judicially unprecedented" because since 2003, FERC, breaking with past practice, has sometimes (though not always) accepted *Mobile-Sierra* provisions in settlements and other contracts that set rates to be paid by contracting and non-contracting wholesale customers alike. Before 2003 (and occasionally since then), FERC rejected such provisions and held *Mobile-Sierra* inapplicable to non-consenting third parties. *E.g.*, *PJM Interconnection, LLC*, 96 F.E.R.C. ¶ 61,206, at 61,878 & n.13 (2001) (holding that "*Mobile-Sierra* does not speak to situations ... where a non-party ... seeks changes under Section 206" and citing cases); *Carolina Power & Light Co.*, 67 F.E.R.C. ¶ 61,074, at 61,205 (1994) (rejecting settlement provisions purporting to hold non-parties to a *Mobile-Sierra* presumption on grounds that they are "contrary to Commission precedent and to the Commission's statutory mandate").

the rates as a result of that acceptance. The issuance of a ruling on this point would resolve the only matter at issue in this proceeding. However, Petitioners have asked the Court to resolve the separate question of whether, in cases where a *Mobile-Sierra* presumption legitimately attaches, that standard applies to a subsequent rate challenge mounted by an indirectly-affected third party, such as a retail customer to whom costs are passed through.

APPA and NRECA submit that there is no single, hard-and-fast rule to be applied. The right answer depends on (*inter alia*): the degree of alignment between the interests of the contracting buyer or seller and that of the complainant and whether the circumstances under which the agreement was negotiated supports a presumption that the rates were reasonable. In many cases, the premise articulated by the amici economists—that "wholesale buyers will seek out the lowest rates" because state regulators may prohibit them from passing-through to retail ratepayers imprudently-incurred costs, Econ. Br. 12—is demonstrably false. *Some* public utilities, including independent system operators such as ISO-NE, are virtually guaranteed to recover from ratepayers *all* of their costs (whether prudently incurred or not) because they are non-profit entities without shareholders and with no other means to cover their costs. As the D.C. Circuit has found, ISO-NE's untrammeled

ability to pass through its costs undercuts confidence that it will seek assiduously to minimize those costs. *NSTAR Elec. & Gas Corp. v. FERC*, 481 F.3d 794, 803 (D.C. Cir. 2007). APPA and NRECA submit that, in such circumstances, FERC may not reasonably presume the justness of the rates that an ISO agrees to pay on behalf of load-side interests but is virtually guaranteed to pass through to its load-serving customers.

Stated differently, situations will arise in which customers who are nominally "indirectly affected," *e.g.*, Petr'rs' Br. 3, are in fact the real parties in interest, even though they were not represented at the bargaining table. At times, FERC itself has recognized that independent system operators' ostensibly bilateral contracts function as tariffs setting market-wide rates or establishing market-wide rules, and it has rejected or modified *Mobile-Sierra* provisions in such contracts,[21] a step that Petitioners' position would

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[21] *E.g.*, *ISO New England Inc.*, 106 F.E.R.C. ¶ 61,280, PP 128-30, *corrected by* 107 F.E.R.C. ¶ 61,051 (2004), *petition for review denied sub nom. Me. Pub. Utils. Comm'n v. FERC*, 454 F.3d 278 (2006); *Bridgeport Energy, LLC*, 118 F.E.R.C. ¶ 61,243, P 41 (2007) (finding that "it would be inconsistent with our duty under the [FPA]" to accept provisions in such contracts purporting to affect the standard of review to be applied to rate-change requests by non-parties or by the Commission *sua sponte*); *PSEG Power Co., LLC*, 119 F.E.R.C. ¶ 61,168, P 25 (2007); *Milford Power Co., LLC*, 119 F.E.R.C.

foreclose. The Court should not adopt any rule regarding ostensible "third parties" that bars FERC from recognizing such distinctions or from conducting an ordinary just-and-reasonable review of contract rates virtually guaranteed to be imposed on customers of independent system operators.

IV. *MAINE PUBLIC* DOES NOT CONFLICT WITH *MORGAN STANLEY'S* HOLDING THAT THERE IS ONLY ONE STATUTORY STANDARD

Petitioners argue that the decision below must be vacated because it conflicts with *Morgan Stanley*'s holding that the FPA contains only one standard by which to judge public utility rates: the just-and-reasonable standard. *E.g.*, Pet'rs' Br. 24-25. That argument should be rejected. While *Maine Public* was decided before *Morgan Stanley* and used pre-*Morgan Stanley* nomenclature, the D.C. Circuit denied FERC's request for rehearing, including rehearing *en banc*, after this Court's decision was issued. None of the nine judges who considered FERC's *en banc* petition voted to rehear the case. Pet'rs' App. 247a. Petitioners' argument that *Maine Public* conflicts with *Morgan Stanley* amounts to an assertion that all nine of those

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¶ 61,167, P 31 (2007).

judges subscribed, even after *Morgan Stanley*, to the "obviously indefensible" proposition (128 S. Ct. 2740) that *Morgan Stanley* rejected.

The reality is that the D.C. Circuit's decision did not depend on treating the public-interest test as a statutory exception. Restating its holding using *Morgan Stanley*'s terminology, *Maine Public* held that contracting parties may not impose rates on unwilling wholesale customers through a contested settlement and then erect a presumption of reasonableness making it harder for them to challenge those rates in light of changed circumstances. That determination was correct and should be affirmed.

CONCLUSION

The decision below should be affirmed because FERC erred in accepting Section 4.C of the contested settlement agreement.

Respectfully submitted,

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AMICUS CURIAE BRIEF

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IN THE

Supreme Court of the United States

NRG POWER MARKETING, LLC, ET AL.,

Petitioners,

v.

MAINE PUBLIC UTILITIES COMMISSION, ET AL.,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF COLIN C. BLAYDON, CHARLES J. CICCHETTI, JEFFREY A. DUBIN, A.J. GOULDING, WILLIAM W. HOGAN, JOSEPH P. KALT, PAUL R. KLEINDORFER, ROBERT J. MICHAELS, CRAIG PIRRONG, VERNON L. SMITH, JAMES L. SWEENEY AND ROBERT D. WILLIG AS *AMICI CURIAE* IN SUPPORT OF PETITIONERS

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QUESTION PRESENTED

Whether the D.C. Circuit erred in holding that the *Mobile-Sierra* doctrine—which prohibits the Federal Energy Regulatory Commission from modifying or abrogating electricity and natural gas contracts unless they are shown to be contrary to the public interest—is inapplicable when a contract is challenged by a non-contracting third party.

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INTEREST OF AMICI[1]

Amici are leading professors and scholars who teach and write on economic issues. Many of them have researched and published analyses of the economics of the electricity industry. Several have also testified in various proceedings about the nature, structure, and appropriate regulation of electricity markets. Certain of the *amici* filed a brief in support of petitioners in *Morgan Stanley Capital Group Inc. v. Public Utility District No. 1 of Snohomish County*, 128 S. Ct. 2733 (2008), explaining that, if not overturned, the Ninth Circuit's decision at issue in that case would erode the contract certainty that plays a crucial role in the proper functioning of the wholesale energy markets.[2] *Amici* are similarly concerned that the decision below will result in long-term harm to the energy markets by impeding the ability of market participants to enter into and rely on contracts.

A summary of the *amici's* qualifications and affiliations is provided as an appendix to this brief. *See*

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[1] The parties have consented to the filing of this brief: a letter of consent from the Solicitor General has been filed herewith and blanket letters of consent were filed with this Court on July 10, 2009 by counsel for the other parties. No counsel for a party authored this brief in whole or in part, and no such counsel or any party made a monetary contribution intended to fund the preparation or submission of the brief. Counsel's fees and expenses incurred to prepare this brief were paid by American Electric Power Service Corp., Iberdrola Renewables, Inc., Powerex Corp., Sempra Generation, Shell Energy North America (US), L.P., and TransCanada Energy Ltd. No other person or entity made a monetary contribution intended to fund the preparation or submission of this brief.

[2] *See* Brief of William J. Baumol *et al.*, as *Amici Curiae* in Support of Petitioners, Nos. 06-1457, 06-1462 (filed Nov. 28, 2007).

App., *infra*, at 1a. *Amici* file this brief as individuals, not on behalf of the institutions with which they are affiliated. None of the *amici* is being compensated in connection with this brief.

SUMMARY OF ARGUMENT

Economists have long recognized that contract stability is essential to the health of the energy industry. Buyers and sellers alike in the wholesale energy markets rely on fixed-price, long-term contracts to insulate themselves against price fluctuations and changing market conditions. This encourages and undergirds investment. The energy industry requires large infusions of capital to build generating and transmission facilities to meet demand, and contracts provide developers, producers and lenders with assured revenue streams that are necessary for investment.

This Court made these same points last year in *Morgan Stanley*. It explained that contracts are a "key source of stability" in the energy industry, and that "'uncertainties regarding rate stability and contract sanctity can have a chilling effect on investments and a seller's willingness to enter into long-term contracts,'" which will "'harm customers in the long run.'" 128 S. Ct. at 2749 (citation omitted). The Court confirmed the continuing vitality of the *Mobile-Sierra* doctrine,[3]

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[3] The *Mobile-Sierra* doctrine takes its name from this Court's decisions in *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332 (1956), and *FPC v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956). *Mobile* involved the Natural Gas Act ("NGA"), while *Sierra* involved the Federal Power Act ("FPA"). Because the relevant provisions of the NGA and FPA are "substantially identical," 350 U.S. at 353, the Court has "cite[d] interchangeably

which is "grounded in the commonsense notion that 'in wholesale markets, the party charging the rate and the party charged [are] often sophisticated businesses enjoying presumptively equal bargaining power, who could be expected to negotiate a "just and reasonable" rate as between the two of them.'" *Id.* at 2746 (quoting *Verizon Commc'ns Inc. v. FCC*, 535 U.S. 467, 479 (2002)) (alterations in original). And it reaffirmed that, as a consequence of the presumptive justness and reasonableness of contracts, under *Mobile-Sierra* the Federal Energy Regulatory Commission ("FERC") has no power to modify a "mutually agreed-upon contract rate" unless the rate "seriously harms the consuming public." *Id.*

This Court's decisions in *Mobile*, *Sierra* and *Morgan Stanley* assure participants in the wholesale energy markets that their contracts will be enforced except in rare "circumstances of unequivocal public necessity." *Permian Basin Area Rate Cases*, 390 U.S. 747, 822 (1968). The regulatory scheme thereby strikes a necessary and appropriate balance: contracting parties transact secure in the knowledge that their bargains will be enforced in all but the most extraordinary circumstances, and consumers are at the same time protected by contracts that provide rate stability and support infrastructure investments and by FERC's ability to override a contract if it "harms the public interest." *Morgan Stanley*, 128 S. Ct. at 2747.

The rule announced by the D.C. Circuit in this case would disrupt that careful balance, destroy the

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decisions interpreting the pertinent sections of the two statutes." *Ark. La. Gas Co. v. Hall*, 453 U.S. 571, 577 n.7 (1981).

contract certainty long fostered by *Mobile-Sierra*, and threaten the health and stability of the energy industry on which the public relies. The D.C. Circuit held that a contract that would be presumed reasonable under the FPA in any challenge by a contracting party loses that presumption if the challenge is instead mounted by a third party, and that third-party challenges are subject to review under the less deferential "'ordinary' 'just and reasonable'" standard that the Commission applies to unilateral rate filings. *Morgan Stanley*, 128 S. Ct. at 2740 (citation omitted). This third-party exception to *Mobile-Sierra* would as a practical matter swallow the rule because an incredibly wide range of third parties—including retail consumers, consumer advocacy groups, and state and local government bodies acting for their constituents—are typically affected by, and thus would have the incentive and standing to challenge, the wholesale contracts for electricity that the Commission regulates.

Reliable contract enforcement is crucial to economic growth and development because contracts provide the most efficient way for parties to allocate the risk of uncertain future market conditions between themselves in a manner that benefits them *and society as a whole*. The D.C. Circuit's third-party exception to the *Mobile-Sierra* presumption is inconsistent with that basic understanding. By empowering all third parties, even those not involved in initial contract negotiations and only indirectly affected by contract terms, to retroactively undo wholesale contracts, the D.C. Circuit's holding will undermine contracting parties' ability to reach bargains in the first instance. And parties' inability efficiently to allocate risk in the long run will increase prices and stifle necessary

investments in needed energy infrastructure, injuring the very public welfare that the statute is intended to safeguard. The same economic rationales that are manifest in *Mobile*, *Sierra*, and *Morgan Stanley* require contracts to be enforced as agreed to by the contracting parties, regardless of whom might later seek to undo them, except when absolutely necessary to protect the public.

ARGUMENT

I. THE *MOBILE-SIERRA* DOCTRINE PROVIDES CONTRACTUAL CERTAINTY CRUCIAL TO THE HEALTH OF THE ELECTRICAL POWER INDUSTRY

Economists have long understood that the law must consistently and predictably enforce the rights and obligations of contracts in order to foster economic development.[4] Parties' ability to rely on contract enforcement is especially crucial in the inherently volatile wholesale electricity markets. Hany A. Shakwy *et al.*, *A First Look at the Empirical Relation*

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[4] *See, e.g.*, Adam Smith, *The Wealth of Nations* 133 (Edwin Cannan ed., Bantam Dell 2003) (1776) ("When the law does not enforce the performance of contracts, it puts all borrowers nearly upon the same footing with bankrupts ...."); Daniel Kaufman *et al.*, World Bank Policy Research Working Paper No. 2196, *Governance Matters* 8, 12 (Oct. 1999) (contract enforceability a key component of the "rule of law," which is critical to economic development); Ross Levine, *The Legal Environment, Banks and Long-Run Economic Growth*, 30 J. Money, Credit and Banking 596, 610-11 (1998) (contract enforceability facilitates the development of efficient banking systems necessary for economic growth); *see also Am. Airlines, Inc. v. Wolens*, 513 U.S. 219, 230 (1995) ("Market efficiency requires effective means to enforce private agreements.").

Between Spot and Futures Electricity Prices in the United States, 23 J. Futures Mkts. 931, 932 (2003). Because electricity cannot be stored, spot prices are vulnerable to spikes in demand. Indeed, a "properly-functioning, fully-competitive electricity market is likely to yield market prices that vary by a factor of ten or twenty to one in a single day." Richard J. Pierce, Jr., *How Will the California Debacle Affect Energy Deregulation?*, 54 Admin. L. Rev. 389, 395 (2002); *see also* Francis A. Longstaff & Ashley W. Wang, *Electricity Forward Prices: A High-Frequency Empirical Analysis*, 59 J. Fin. 1877, 1877 (2004) (lack of storage capability makes electricity vulnerable to price fluctuations); Energy Information Administration, U.S. Dep't of Energy, *Derivatives and Risk Management in the Petroleum, Natural Gas and Electricity Industries* 1 (Oct. 2002) ("[E]nergy prices are among the most volatile of all commodities ....").[5] Long-term contracts allow participants in the electricity markets to manage efficiently the risks associated with that extreme volatility.

More particularly, long-term contracts assure buyers of steady supplies at fixed or stable costs, allowing them to avoid exposure to unpredictable spot prices. *See* John C. Hull, *Options, Futures, and Other Derivatives* 9-10 (6th ed. 2006). At the same time, long-term contracts give sellers the certainty and stability necessary to incentivize optimal investments in our power infrastructure. The electric industry is "inherently capital-intensive." Amy Abel, CRS Report for Congress, *Electric Transmission: Approaches for*

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[5] *Available at* http://www.eia.doe.gov/oiaf/servicerpt/derivative/.

Energizing a Sagging Industry 1 (Oct. 2007).[6] The building or upgrading of electric generating and transmission facilities often requires hundreds of millions of dollars. Once such capital is invested, "the resulting assets are typically immobile and suitable only to a single purpose," and the investor therefore "cannot easily exit the business without losing these massive sunk costs." William P. Barr *et al.*, *The Gild That Is Killing the Lily: How Confusion Over Regulatory Takings Doctrine Is Undermining the Core Protections of the Takings Clause*, Geo. Wash. L. Rev. 429, 441-42 (2005). Long-term contracts encourage investment by reducing developers' and lenders' risks that they will fail to recoup their investments over time. By agreeing to long-term contracts, both buyers and sellers are able to hedge against future uncertainty by locking-in stable prices.

The volatility that encourages parties to enter into contracts in the first instance may of course result in a contracting party later being "out-of-the-money," with an incentive to seek to overturn the bargain. Knowing that, parties will not enter into contracts unless they are confident that the law will uphold their agreements in the face of changing and unpredictable market conditions. Economists have thus emphasized the importance of regulatory certainty to the continued development of the industry. *See, e.g.*, Mario Bergara *et al.*, *Political Institutions and Electric Utility Investment: A Cross-Nation Analysis*, 40 Cal. Mgmt. Rev. 18, 19-20 (1998); Mark A. Jamison *et al.*, *Measuring and Mitigating Regulatory Risk in Private*

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[6] *Available at* http://nceonline.org/NLE/CRSreports/06Oct/RL32075.pdf

Infrastructure Investment, 18 Elec. J. 36, 37 (2005); Pablo T. Spiller, *A Positive Political Theory of Regulatory Instruments: Contracts, Administrative Law or Regulatory Specificity?*, 69 S. Cal. L. Rev. 477, 482-83 (1996). As the D.C. Circuit previously recognized, "'[t]he certainty and stability which stems from contract performance and enforcement is essential to an orderly bulk power market. If the integrity of contracts is undermined, business would be transacted without legally enforceable assurances and we believe that the market, the industry and ultimately the consumer would suffer.'" *San Diego Gas & Elec. Co. v. FERC*, 904 F.2d 727, 730 (D.C. Cir. 1990) (citation omitted).

Congress appreciated these dynamics and enacted a regulatory scheme that accommodates the freedom and obligations of contract. The FPA "evince[d] no purpose to abrogate private rate contracts as such," *Mobile*, 350 U.S. at 338, and left unchanged the powers of public utilities "to establish *ex parte*, and change at will, the rates offered to prospective customers; or to fix by contract, and change only by mutual agreement, the rate agreed upon with a particular customer." *Id.* at 343. Although the FPA requires that all rates for electricity be "just and reasonable," 16 U.S.C. § 824e(a), rates set by contract require a "differing *application*" of the just and reasonable standard. *Morgan Stanley*, 128 S. Ct. at 2740. Under the *Mobile-Sierra* doctrine, contract rates are presumed to be just and reasonable, and that presumption may be overcome only if the rate "seriously harms the consuming public." *Id.* at 2746; *see also Sierra*, 350 U.S. at 355 (Commission may only modify a rate that "adversely affect[s] the public interest"). In this way,

the Act is interpreted to "afford[] a reasonable accommodation between the conflicting interests of contract stability on the one hand and public regulation on the other." *Mobile*, 350 U.S. at 344. By establishing a "high" standard for regulatory modification of contracts, *Morgan Stanley*, 128 S. Ct. at 2749 n.6, the *Mobile-Sierra* doctrine provides the regulatory certainty that is necessary to support the efforts of market participants to allocate risks between themselves by contract.

II. THERE IS NO ECONOMIC BASIS FOR A THIRD-PARTY EXCEPTION TO THE *MOBILE-SIERRA* PUBLIC INTEREST STANDARD

In *Morgan Stanley*, this Court affirmed the centrality of *Mobile-Sierra*'s presumption of reasonableness to the FPA's regulatory scheme. *See* 128 S. Ct. at 2749 ("The FPA recognizes that contract stability ultimately benefits consumers, even if short-term rates for a subset of the public might be high by historical standards ...."). The D.C. Circuit's decision below would effectively eliminate that presumption. The D.C. Circuit held unequivocally that "the *Mobile-Sierra* doctrine *simply does not apply*" in any circumstances where "a rate challenge is brought by a non-contracting third party." Pet. App. 22a (emphasis added).

The D.C. Circuit's decision to exempt all third parties from the *Mobile-Sierra* presumption apparently stems from two related erroneous beliefs: first, that a wholesale contract that is presumptively reasonable as between the parties because of the "superior efficiency

of private bargaining" (Pet. App. 19a) is not presumptively reasonable as to third parties; and, second, that the application of the *Mobile-Sierra* presumption to third parties deprives them of their right to a just and reasonable rate. Pet. App. 22a. In so holding, the court of appeals ignored both the underlying economic rationale for freedom of contract and the fact that the *Mobile-Sierra* public interest standard is constructed precisely to permit FERC to modify contract rates when necessary to protect the interest of non-contracting third parties.

Contract law and economic theories of contract rest on the common understanding that, because of the efficiency of private bargaining, buyers and sellers are able to negotiate contracts that maximize gains not only for themselves but also for society as a whole. *See, e.g.*, Anthony T. Kronman & Richard A. Posner, *The Economics of Contract Law* 2 (1979) (voluntary exchanges "facilitate[] the allocation of the good or service in question to the use in which it is most valuable, thereby maximizing the wealth of society"); Richard A. Posner, *Economic Analysis of Law* 14 (4th ed. 1992) ("Where resources are shifted pursuant to" a contract, "we can be reasonably sure that the shift involves an increase in efficiency."); Charles J. Goetz & Robert E. Scott, *Enforcing Promises: An Examination of the Basis of Contract*, 89 Yale L.J. 1261, 1265 (1980) ("Bargained-for promises support value-enhancing exchanges."); Morton J. Horwitz, *The Historical Foundations of Modern Contract Law*, 87 Harv. L. Rev. 917, 947 (1974) ("The role of contract law [is] simply to enforce ... transactions that parties to a contract believed to be to their mutual advantage."); Daniel Markovits, *Making and Keeping Contracts*, 92

Va. L. Rev. 1325, 1332-33 (2006) (economic theory views contracts as "allow[ing] persons to coordinate their conduct to their joint advantage"); Susan Randall, *Freedom of Contract in Insurance*, 14 Conn. Ins. L.J. 107, 122 (2007-2008) (the "principle of freedom of contract" rests, in part, on the view that "individual choice furthers an efficient market, maximizing individual and social utility"); *see also* Richard J. Pierce, *Reconsidering the Roles of Regulation and Competition in the Natural Gas Industry*, 97 Harv. L. Rev. 345, 356 (1983) ("Long-term contracts allow parties to bargain for the socially optimum mix of price and supply security.").

The efficiency benefits of contract are especially obvious in the wholesale electric industry, where buyers and sellers are "sophisticated businesses enjoying presumptively equal bargaining power." *Verizon*, 535 U.S. at 479. Sophisticated participants in the wholesale energy markets make the decision to contract based on their best projections of future market conditions. In making these projections, they rely on a wide array of information, including the projected growth of demand over time, the amount of new supply that is under development, and the anticipated price of fuel and emissions credits. Because much of this information is publicly available, economic theory recognizes that neither the buyer nor the seller will be able to realize substantial advantages over one another or, indeed, over the market as a whole. *See, e.g.*, Benjamin E. Hermalin & Michael L. Katz, *Judicial Modification of Contracts Between Sophisticated Parties: A More Complete View of Incomplete Contracts and Their Breach*, 9 J.L. Econ. & Org. 230, 244 (1993) ("[T]he legal system can do no better than to

grant complete freedom of contract" to parties that are "symmetrically informed at the time that they reach the initial agreement."); Alan Schwartz & Robert E. Scott, *Contract Theory and the Limits of Contract Law*, 113 Yale L.J. 541, 554 n.24 (2003) (even the existence of asymmetric information will result in contracts that "are efficient given the information structure facing the parties" and "the state seldom can improve on constrained efficient contracts because information that was unavailable to the parties is unlikely to be available to the decisionmaker"); *cf. Basic Inc. v. Levinson*, 485 U.S. 224, 247 (1988) (recognizing that "most publicly available information is reflected in market price").

Moreover, sophisticated buyers and sellers bargaining at arm's length have the incentive and ability to strike a deal that is congruent with the interests of the consuming public. Long-term wholesale power contracts ensure that retail customers, as well as buyers themselves, will be able to obtain reliable supplies at predictable and controlled rates. In negotiating their contracts, wholesale buyers will seek out the lowest rates because they may be prohibited by state regulators from passing-through to their retail customers costs that were not prudently incurred.[7] Conversely, sellers will refrain from

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[7] In setting retail rates, state commissions cannot question the reasonableness of rates approved by FERC, but they do retain their authority to disapprove the pass-through of purchasing costs that were not prudent. *See, e.g., Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953, 972 (1986) ("[W]e may assume that a particular *quantity* of power procured by a utility from a particular source could be deemed unreasonably excessive if lower cost power is available elsewhere, even though

attempting to charge exorbitant rates because they know that they must compete with other producers to make sales and that anticompetitive conduct is subject to regulatory and antitrust oversight. Furthermore, with the advent of market-based pricing, *see Morgan Stanley*, 128 S. Ct. at 2740-42, sellers have no guarantee of cost recovery and must instead rely on their competitive sales to generate profits. Accordingly, parties in the wholesale energy markets

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the higher cost power actually purchased is obtained at a FERC-approved, and therefore reasonable, *price*."); *Miss. Power & Light Co. v. Mississippi*, 487 U.S. 354, 373-74 (1988) ("[I]t might well be unreasonable for a utility to purchase unnecessary quantities of high-cost power, even at FERC-approved rates, if it had the legal right to refuse to buy that power."); *Ky. W. Va. Gas Co. v. Pa. PUC*, 837 F.2d 600, 609 (3d Cir.) ("[A] state cannot independently pass upon the reasonableness of a wholesale rate on file with FERC" but "a state commission may legitimately inquire into whether the retailer prudently chose to pay the FERC-approved wholesale rate of one source, as opposed to the lower rate of another source."), *cert. denied*, 488 U.S. 941 (1988); *Commonwealth Elec. Co. v. Dep't of Pub. Utils.*, 491 N.E.2d 1035, 1045 (Mass. 1986) ("[W]hile the [Department of Public Utilities] cannot inquire into the reasonableness of wholesale rates fixed by FERC, the DPU may inquire whether a purchaser ... is warranted in agreeing to purchase at such a rate considering its alternatives.") (citation omitted), *cert. denied*, 481 U.S. 1036 (1987); *Pike County Light & Power Co. v. Pa. PUC*, 465 A.2d 735, 738 (Pa. Commw. Ct. 1983) (FERC focuses on "whether it is just and reasonable for [a seller] *to charge* a particular rate, but makes no determination of whether it is just and reasonable for [the buyer] *to incur* such a rate as an expense"). Prudence reviews by state commissions provide an additional level of protection to retail customers by ensuring that buyers have struck a reasonable bargain at the time of contracting. This approach is consistent with the principles underlying *Mobile-Sierra*: regulators are not permitted to undermine the integrity of contracts, but may require buyers to bear fully the costs of their "improvident bargains." *Sierra*, 350 U.S. at 355.

should be expected to reach allocations of risk and reward that, over the long haul, are economically efficient as to third parties, and to do so without incurring the enormous transaction costs associated with a bargaining process that included all third parties that may ultimately be affected by a contract.

In light of these principles, this Court rightly recognized in *Morgan Stanley* that a negotiated contract rate is presumptively "just and reasonable" not only as to the contracting parties but also as to the Commission, the quintessential third party charged by Congress with the protection of the public interest. *See* 128 S. Ct. at 2746 ("*Sierra* ... provided a definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context."). The *Mobile-Sierra* presumption of justness and reasonableness is, indeed, fundamentally a limitation on the Commission's own authority to upset voluntary contractual bargains. *Id.* ("[O]nly when the mutually agreed-upon contract rate seriously harms the consuming public may the Commission declare it not to be just and reasonable.").

Because the *Mobile-Sierra* presumption is premised on the agreement of willing and sophisticated parties, the Commission retains "ample authority to set aside a contract where there is unfair dealing at the contract formation stage—for instance, if it finds traditional grounds for the abrogation of the contract such as fraud or duress" or if "'dysfunctional' market conditions under which the contract were formed" were the directly caused result of illegal market manipulation by one of the contracting parties. *Id.* at 2747. For the same reason, the *Mobile-Sierra* doctrine would not be

interpreted to permit one party to "thrust" unilaterally upon others terms to which they "have vociferously objected." Pet. App. 22a.[8]

The *Mobile-Sierra* doctrine also provides the Commission ample tools to protect the interests of non-contracting third parties where there has been no unfair dealing at the contract formation stage. Indeed, the "sole concern" of the Commission when faced with a valid, voluntarily negotiated contract is the protection of the public interest. *Morgan Stanley*, 128 S. Ct. at 2746 n.3 (citing *Sierra*, 350 U.S. at 355). But the governmental power to undo otherwise valid contracts in the public interest must be exercised with great restraint. As this Court has long recognized, private contracts will always "in some respect, however slight, affect the public," *Nebbia v. New York*, 291 U.S. 502, 524-25 (1934), but even in the case of "businesses affected with a public interest" regulation must reflect a "reasonable exertion of governmental authority." *Id.* at 536; *see also Chas. Wolff Packing Co. v. Court of Indus. Relations*, 262 U.S. 522, 536 (1923) ("[T]he mere declaration ... that a business is affected with a public interest is not conclusive of the question whether ... attempted regulation on that ground is justified."). To preserve the long-term benefits that

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[8] Despite its stated concern about such cram-downs, the D.C. Circuit made no attempt to tailor its holding to situations where there is no contractual agreement whatsoever, or, as with the contested settlement agreement in the case below (*see* Pet. App. 5a), where agreement is only reached by a subset of the negotiating parties. Instead, the court of appeals categorically held that the *Mobile-Sierra* doctrine is simply inapplicable where *any* non-contracting third party seeks to challenge the terms of an existing contract. Pet. App. 22a.

contracts provide to market participants and the industry as a whole, "the FPA intended to reserve the Commission's contract-abrogation power for those *extraordinary* circumstances where the public will be *severely* harmed." *Morgan Stanley*, 128 S. Ct. at 2749 (emphasis added).

In this case, the D.C. Circuit went far beyond what is necessary to ensure the "existence of a voluntary contract between the parties," Pet. App. 21a, to protect the integrity of the contracting process, or to protect the public from extraordinary harm: Even where there is a valid bilateral or multilateral agreement, it held that the *Mobile-Sierra* doctrine "simply does not apply" if the agreement is later challenged by any third party. Pet. App. 22a. In the D.C. Circuit's view, the *Mobile-Sierra* public interest standard does not adequately protect the public. Ignoring the fact that "contract stability ultimately benefits consumers," *Morgan Stanley*, 128 S. Ct. at 2749, the court of appeals held that third parties should be completely exempted from the restrictions of the *Mobile-Sierra* doctrine because they need the ability "successfully [to] challenge rates in cases of changed circumstances." Pet. App. 23a.

The D.C. Circuit's approach gives "short shrift to the important role of contracts in the FPA." *Morgan Stanley*, 128 S. Ct. at 2749. Although there will always be a "winner" and a "loser" given the difficulty in perfectly predicting future market conditions, this does not justify relieving sophisticated buyers and sellers—or third parties indirectly affected by their bargain—of the consequences of informed and voluntary contracting decisions. Contracts are a necessary and

valuable risk-management tool precisely because parties understand that their market projections may later prove inaccurate and therefore seek efficiently to allocate the risk of "changed circumstances" among themselves. Thus, "a fixed-price contract is an explicit assignment of the risk of market price increases to the seller and the risk of market price decreases to the buyer." *N. Ind. Pub. Serv. Co. v. Carbon County Coal Co.*, 799 F.2d 265, 278 (7th Cir. 1986); *see also* Posner, *supra*, at 119 (because "an important function of contracts is to assign risks to superior risk bearers," the party assigned the risk "must pay" when "the risk materializes"). Because contracting parties have allocated the risk of price fluctuations between themselves and will organize their affairs in reliance on their contractual bargains, economists have long recognized that it would be counterproductive and injurious to consumer welfare to invite contract modification whenever market prices do not turn out as expected.[9] Contrary to the D.C. Circuit's

[9] *See, e.g.*, Schwartz & Scott, *supra*, 113 Yale L.J. at 565 ("[W]ithout legal enforcement, private contracting parties cannot be expected often to create deals that maximize social surplus."); Goetz & Scott, *supra*, 89 Yale L.J. at 1270 (where contract performance is uncertain, a party will limit its behavior adjustments, thereby giving up "the value of the prospective beneficial reliance that would accrue from full adaptation to the advance knowledge of a promissory performance"); *id.* at 1274 ("Precautionary adjustments by the promisor decrease the value of the promise."); Daniel A. Farber, *Contract Law and Modern Economic Theory*, 78 Nw. U. L. Rev. 303, 315-18 (1983); *cf.* Posner, *supra*, at 93 (the goal of efficiency is furthered by "enforcing the parties' agreement" even if it later "appears to be inefficient"). The courts have similarly emphasized that it is not the role of the government to relieve contracting parties of "hard bargains" resulting from their "indiscretions and bad judgments" as such governmental intrusion into contractual relations would

understanding, *Mobile-Sierra* limits FERC's ability to modify contracts not as an accommodation to the parties but for the benefit of the public as a whole.

III. THE D.C. CIRCUIT'S BROAD THIRD-PARTY EXCEPTION WOULD DESTROY THE CONTRACTUAL CERTAINTY NECESSARY FOR THE EFFICIENT FUNCTIONING AND DEVELOPMENT OF THE ELECTRICAL POWER INDUSTRY

Because virtually every wholesale energy contract affects a vast number of downstream third parties, a presumption of justness and reasonableness that applied only to the contracting parties themselves would be "no presumption of validity at all, but a reinstitution of cost-based rather than contract-based regulation." *Morgan Stanley*, 128 S. Ct. at 2748. If upheld, the D.C. Circuit's third-party exception to the *Mobile-Sierra* presumption will undermine the faith in contractual certainty that lies at the heart of the doctrine and enables the efficient allocation of risk necessary to the effective operation and development of the energy industry.

Parties entering into contracts rely on the understanding that, under traditional contract law

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"create an insecurity in business transactions which would be intolerable." *Wilmington & Weldon R.R. Co. v. King*, 91 U.S. (1 Otto) 3, 5 (1875); *see also Ark. Natural Gas Co. v. Ark. R.R. Comm'n*, 261 U.S. 379, 383 (1923) ("[I]t is not an independent legislative function to vary or set aside ... contracts, however unwise and unprofitable they may be."); *N. Ind. Pub. Serv. Co.*, 799 F.2d at 278 ("If ... the buyer forecasts the market incorrectly and therefore finds himself locked into a disadvantageous contract, he has only himself to blame ....").

principles, their rights and obligations are defined by the terms of their contracts, safe from third party interference. *See, e.g., Williams v. Eggleston*, 170 U.S. 304, 309 (1898) ("The parties to a contract are the ones to complain of a breach, and ... a third party has no right to insist that it has been broken."); *United Steelworkers of Am. v. Rawson*, 495 U.S. 362, 375 (1990) ("[T]hird-party beneficiaries generally have no greater rights in a contract than does the promisee.").

Parties contracting in the wholesale energy markets have long relied on the same expectation. Indeed, the *Mobile-Sierra* doctrine acts principally as a limitation on interference by the Commission—the ultimate third-party enforcer charged by Congress with oversight of wholesale rates for the public benefit. The Commission is "*required* ... to apply the *Mobile-Sierra* presumption in its evaluation" of fixed-price, long-term contracts, regardless of when it is asked to undertake such a review. *Morgan Stanley*, 128 S. Ct. at 2745. This limitation appropriately bars FERC (itself a third party) from applying a hindsight notion of what would have been a "reasonable" contract rate, and instead ensures that the voluntary bargains struck by the parties at the time of contracting are respected. The D.C. Circuit's holding, however, would provide any other third party the unbounded ability to demand review of contract rates free of the presumption of reasonableness.

The D.C. Circuit's third-party exception would invite frequent and wholesale *ex post* regulatory interference with voluntarily negotiated contracts. The D.C. Circuit made no effort to confine its holding to the situation before it. Under the court of appeals'

holding, even when parties have voluntarily assented to the terms of a contract, their agreement is not safe from third party challenge, regardless of whether the challenger participated in contract negotiations but refused to agree, or is only indirectly affected by the contract. But the FPA governs "the business of transmitting and selling electric energy for ultimate distribution to the public." 16 U.S.C. § 824(a). Every wholesale contract reviewed by the Commission affects retail customers down the line, and there will accordingly *always* be some customer or consumer advocate with an interest in relieving a buyer of a contract rate that, in hindsight, appears too high. A seller competing for a buyer's business will also have an incentive to exploit the third-party exception and break existing contractual obligations so that the buyer is free to seek alternative sources of supply. And the FPA's liberal standing rules would give all of them the right to launch such *ex post* challenges. *See* discussion of standing in Brief of the Electric Power Supply Association, *et al.* as *Amici Curiae* in Support of the Petition for Certiorari at 8-9, No. 08-674 (filed Dec. 22, 2008) ("EPSA Brief").

State regulators and consumer advocates have already demonstrated their zeal to challenge in hindsight the reasonableness of contract rates agreed to by sophisticated buyers and sellers. For example, in a companion case to *Morgan Stanley*, two California state agencies purporting to act in the interest of the State's retail customers filed complaints with FERC seeking to lower the long-term contract rates agreed to by their sister agency, the California Department of Water Resources, when contracting for the benefit of those same retail customers. *See Pub. Utils. Comm'n*

of Cal. v. Sellers of Long Term Contracts to the Cal. Dep't of Water Res., 103 F.E.R.C. ¶ 61,354, *order on reh'g*, 105 F.E.R.C. ¶ 61,182 (2003), *remanded sub nom. Pub. Utils. Comm'n of Cal. v. FERC*, 474 F.3d 587 (9th Cir. 2006), *vacated and remanded sub nom. Sempra Generation v. Pub. Utils. Comm'n of Cal.*, 128 S. Ct. 2993 (2008), *and vacated and remanded, Pub. Utils. Comm'n of Cal. v. FERC*, 550 F.3d 767 (9th Cir. 2008). Although this Court vacated and remanded the Ninth Circuit's decision in their favor in light of *Morgan Stanley*, those state agencies are currently arguing before the Commission that their challenge should not be governed by *Morgan Stanley*, or *Mobile-Sierra* principles generally, because—since a different California agency was the signatory to the contracts—the two challengers are "third parties." *See* Answer and Cross-Motion of the Public Utilities Commission of the State of California for an Order Governing Procedures on Remand, FERC Docket Nos. EL02-60-003 *et al.*, at 22-26 (filed Jan. 14, 2009); Answer of the Public Utilities Commission of the State of California to Cross Motion of Sempra Generation and Cross Motion for Summary Disposition, FERC Docket Nos. EL02-60-003 *et al.* (filed Jan. 21, 2009); Motion for Leave to Answer of the Public Utilities Commission of the State of California and Answer of the Public Utilities Commission of the State of California to Answer of Indicated Sellers and Answer of Sempra Generation, FERC Docket Nos. EL02-60-003 *et al.* (filed Feb. 9, 2009). The Illinois Attorney General also filed a complaint with FERC seeking to abrogate wholesale contracts awarded to sellers submitting the lowest bids in a descending clock auction supervised by state utility regulators and economic experts. *See* Amended Complaint by the People of the State of

Illinois *ex rel.* Illinois Attorney General Lisa Madigan, FERC Docket No. EL07-47-000 (filed Mar. 16, 2007); *see also* Section 206 Complaint, FERC Docket No. EL07-50-000 (filed Mar. 26, 2007) (complaint by California consumer group challenging contract). Such challenges will only become more common if petitions by downstream consumers and their representatives are not subject to the strictures of the *Mobile-Sierra* doctrine.

If the D.C. Circuit is upheld, parties seeking to allocate risk between themselves through contract will routinely be forced to attempt to negotiate terms and conditions that account for potential contract challenges by non-contracting third parties who are not present at the negotiating table. This would greatly complicate contractual bargaining, vastly increase transaction costs, and despite the parties' best efforts, expose their bargains to potentially endless litigation by a wide array of third parties.

These developments would be all the more harmful because their effects would almost surely prove asymmetrical. In theory, the D.C. Circuit's third-party exception would allow parties with an interest in a seller's financial health (*e.g.*, the seller's shareholders, lenders and suppliers) to bring contract challenges against rates that in hindsight appear too low. As a practical matter, however, some may argue that such entities are not true third parties with independent standing. Any third-party exception is therefore very likely to be a one-way ratchet, allowing buyers, but not sellers, to be relieved of contractual bargains that later prove unprofitable. *But see Morgan Stanley*, 128 S. Ct. at 2747 ("The standard for a buyer's challenge must be

the same, generally speaking, as the standard for a seller's challenge: The contract rate must seriously harm the public interest.").

At a minimum, sellers faced with the threat of asymmetrical contract modification will demand a substantial premium to compensate for the risk that consumers or their proxies will later challenge contract rates as being too high. *See, e.g.*, *Standard of Review for Proposed Changes to Market-Based Rate Contracts for Wholesale Sales of Elec. Energy by Pub. Utils.*, 100 F.E.R.C. ¶ 61,145, at 61,545 (2002) ("Investors will not participate in a market in which disgruntled buyers are allowed to break their contracts, at least not without charging a significant risk premium.") (Brownell and Breathitt, Commissioners, concurring); *see also Puget Sound Energy, Inc. v. All Jurisdictional Sellers of Energy and/or Capacity at Wholesale into Elec. Energy and/or Capacity Markets in the Pac. Northwest*, 103 F.E.R.C. ¶ 61,348, at 62,368-69 (2003) (threat of refunds "would cause a loss of confidence in the market, have a chilling effect on trading, cause costs to customers to increase as market participants demand additional risk premiums and additional security for their transactions, create a hesitancy to conduct business in times of scarcity, and discourage investment in needed infrastructure"); *Cal. Indep. Sys. Operator Corp.*, 108 F.E.R.C. ¶ 61,254, at 62,409-10 (2004) (explaining that a methodology that "reduc[es] cost uncertainty and the corresponding need for a risk premium" reduces costs to consumers).[10] At worst,

[10] In the underlying proceedings before the Commission, various parties explained that the *Mobile-Sierra* provision in the contested settlement agreement was intended to "reduce regulatory uncertainty and the risk premium that may be

because the very purpose of long-term contracts is to allow parties to hedge the risk of market fluctuations, an asymmetrical standard that encourages third party retail customers or their representatives to challenge contracts deemed to be "out-of-the-money" after the fact could cause sellers to abandon the market for long-term contracts altogether. *See, e.g.*, Posner, *supra*, at 8 ("If a party for whom a contract to which he freely agreed turns out badly is allowed to revise the terms of the contract ex post, few contracts will be made."); Kronman & Posner, *supra*, at 4 (same). Both results would be economically inefficient and would harm consumers over the long-run: consumers will be either asked to bear costly risk premiums, or the market will be deprived of rate-stabilizing contracts necessary for investment in infrastructure.

Far from the beneficial safety net imagined by the D.C. Circuit, a third-party exception would ultimately harm the public. It would arm third parties who have not sunk their own capital into investments with the right to interfere with mutually agreed-upon contracts. Such parties' private incentives would generally be to seek contract modification or abrogation so as to secure better terms for themselves on the backs of others' sunk investments. A multiplication of these challenges would weaken the ability of wholesale buyers and sellers to rely on long-term contracts and hinder needed investments, imposing external costs across the

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required by new entrants." Pet. App. 196a. The Commission agreed that "[s]tability is particularly important in this case, which was initiated in part because of the unstable nature of ... revenues and the effect that has on generating units." Pet. App. 202a.

entire public. This is the antithesis of an efficient marketplace.

These threats are not merely theoretical or abstract. Because electric generation "project funding [in today's competitive markets] is based on anticipated market-based projections of costs, revenues and relevant risk factors," Electric Energy Market Competition Task Force, *Report to Congress on Competition in the Wholesale & Retail Markets for Electric Energy Pursuant to Section 1815 of the Energy Policy Act of 2005* 78 (Apr. 2007),[11] long-term contracts are "critical in obtaining financing for new generation and ensuring adequate supplies for retail loads at predictable prices." *Id.* at 4. Indeed, FERC has recognized that "[c]ompetitive power markets simply cannot attract the capital needed to build adequate generating infrastructure without regulatory certainty, including certainty that the Commission will not modify market-based contracts unless there are *extraordinary* circumstances." *Pub. Utils. Comm'n of Cal. v. Sellers of Long Term Contracts to the Cal. Dep't of Water Res.*, 99 F.E.R.C. ¶ 61,087, at 61,383 (2002). At the same time, and as explained in the EPSA Brief, approximately $400 billion in electric infrastructure investment is required over the next 15 years. EPSA Brief at 10-11 (citations omitted). By lowering the bar for third-party challenges to voluntarily-struck bargains, the D.C. Circuit's broad third-party *Mobile-Sierra* exception would erode contract certainty and deter parties from entering into the contracts necessary for rate stability and infrastructure

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[11] *Available at* http://www.ferc.gov/legal/fed-sta/ene-pol-act/epact-final-rpt.pdf.

investment precisely at the time when they are most needed.

CONCLUSION

For the foregoing reasons, the D.C. Circuit's decision should be reversed.

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AMICUS CURIAE BRIEF

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Supreme Court of the United States

NRG POWER MARKETING, LLC, ET AL.,

v.

MAINE PUBLIC UTILITIES COMMISSION, ET AL.,

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF THE ELECTRIC POWER SUPPLY ASSOCIATION, COLORADO INDEPENDENT ENERGY ASSOCIATION, ELECTRIC POWER GENERATION ASSOCIATION, INDEPENDENT ENERGY PRODUCERS ASSOCIATION, INDEPENDENT PETROLEUM ASSOCIATION OF AMERICA, INDEPENDENT POWER PRODUCERS OF NEW YORK, INTERSTATE NATURAL GAS ASSOCIATION OF AMERICA, NATURAL GAS SUPPLY ASSOCIATION, NEW ENGLAND POWER GENERATORS ASSOCIATION, INC., NORTHEAST ENERGY AND COMMERCE ASSOCIATION, NORTHWEST & INTERMOUNTAIN POWER PRODUCERS COALITION, PJM POWER PROVIDERS GROUP, AND WESTERN POWER TRADING FORUM AS *AMICI CURIAE* IN SUPPORT OF PETITIONERS

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QUESTION PRESENTED

This Court's recent decision in *Morgan Stanley Capital Group Inc. v. Public Utility District No. 1 of Snohomish County*, 128 S. Ct. 2733 (2008), reaffirmed that, under the *Mobile-Sierra* doctrine, the Federal Energy Regulatory Commission "must presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law," and that the "presumption may be overcome only if" the Commission "concludes that the contract seriously harms the public interest." *Id.* at 2737. In conflict with *Morgan Stanley*, the D.C. Circuit below held that "when a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply." Pet. App. 22a.

The question presented is:

Whether the Commission's authority to abrogate wholesale power contracts is constrained by the *Mobile-Sierra* doctrine when a contract rate is challenged by a non-contracting third party.

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INTEREST OF *AMICI CURIAE*[1]

Amici and their members represent a diverse array of participants in the Nation's electric and natural gas industries that are directly affected by the issues raised in this case. *Amici*'s members have made long-term financial commitments, involving hundreds of billions of dollars, in reliance on this Court's settled authorities protecting the integrity of privately negotiated wholesale power contracts. Because the D.C. Circuit's decision undoes much of this Court's work in *Morgan Stanley Capital Group Inc. v. Public Utility District No. 1 of Snohomish County*, 128 S. Ct. 2733 (2008), and purports to grant the Federal Energy Regulatory Commission never-before-recognized authority to abrogate contracts challenged by non-contracting third parties, *amici* are concerned that, if left standing, the decision below will destabilize the Nation's power markets, discourage much-needed investment, and ultimately lead to higher costs for consumers.

The Electric Power Supply Association **("EPSA").** EPSA is a national trade association representing competitive electric power suppliers, including independent power producers, merchant generators, and power marketers. EPSA's mission

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[1] The parties have consented to the filing of this brief in letters on file in the Clerk's office. Pursuant to S. Ct. R. 37.6, *amici* state that no counsel for any party authored this brief in whole or in part, and no person or entity, other than *amici* and its counsel, made a monetary contribution intended to fund the preparation or submission of this brief.

is to promote legislative and regulatory policies encouraging a competitive market for electricity.

Colorado Independent Energy Association **("CIEA").** CIEA is a trade association of competitive independent power producers operating in Colorado. Its 34 members and 12 associate members are an integral part of Colorado's energy industry, producing electricity with clean, efficient natural gas-fired cogeneration and renewable technologies.

Electric Power Generation Association **("EPGA").** EPGA is a regional trade association of major electric generating companies that supply wholesale power in Pennsylvania and surrounding states. Its member companies collectively own and operate more than 141,000 megawatts of generating capacity.

Independent Energy Producers Association **("IEP").** IEP is a California non-profit mutual benefit corporation whose members collectively own and operate approximately one-third of California's installed generating capacity.

Independent Petroleum Association of American **("IPAA").** IPAA is a national association representing thousands of independent oil and natural gas producers and service companies across the United States.

Independent Power Producers of New York **("IPPNY").** IPPNY is a not-for-profit trade association representing more than 100 independent power producers involved in the development of generation, and the marketing, and

sale of electric power and natural gas in the State of New York.

Interstate Natural Gas Association of America **("INGAA").** INGAA is a trade association that represents virtually all of the interstate natural gas transportation pipeline and interstate natural gas storage companies operating in the United States, as well as comparable companies in Canada and Mexico. Its members transport over 95 percent of the Nation's natural gas through a network of 220,000 miles of pipelines.

Natural Gas Supply Association **("NGSA").** NGSA is a trade association that represents U.S.-based producers and marketers of natural gas on issues that broadly affect the natural gas industry. NGSA is the voice of suppliers who find, sell, transport, and deliver approximately 30 percent of the United States' natural gas supply.

New England Power Generators Association, Inc. **("NEPGA").** NEPGA is a trade association representing electric generating companies in New England. Its member companies account for approximately 26,000 megawatts of generating capacity in the region.

Northeast Energy and Commerce Association **("NECA").** NECA is a trade association serving New England's competitive electric power industry. Its 800 members include developers and owner/operators of competitive power projects, power marketers and traders, fuel and equipment suppliers, power consumers, and various service providers to the power industry.

Northwest & Intermountain Power Producers Coalition **("NIPPC").** NIPPC represents developers, owners, and operators of non-utility power plants in the Pacific Northwest and Intermountain region.

PJM Power Providers Group **("P3").** P3 is a nonprofit Delaware Corporation whose members serve nearly 12.2 million customers, employ more than 55,000 people, and own more than 75,000 megawatts of power and over 51,000 miles of transmission lines in the thirteen states and the District of Columbia that comprise the PJM Interconnection, LLC region.

Western Power Trading Forum **("WPTF").** WPTF is a California non-profit, mutual benefit corporation that supports the development of uniform operating rules and competitive electricity markets throughout Western electric markets.

INTRODUCTION AND SUMMARY OF ARGUMENT

This case arises out of a carefully negotiated settlement designed to remedy deficiencies in the New England wholesale energy market and to ensure that utilities operating in that market have sufficient electrical generating capacity to satisfy customer demand. The settlement establishes new market rules and an auction process through which rates will be fixed in binding commitments to buy and sell capacity. *See* Pet. Br. 8-12; U.S. Br. 9-12.

The settlement describes the legal standards that, once the settlement is approved by the Commission, will apply to any future complaints challenging (i) the new market rules, (ii) the agreed-on rates that apply during a transition period, or (iii) the contracts to purchase and sell capacity that ultimately result from the auction process. In particular, the settlement includes what is known as a *Memphis* clause, stating that the new market rules may be modified prospectively as long as any modifications are "just and reasonable" as required under the Federal Power Act. *See* 16 U.S.C. § 824d(a). In addition, the settlement includes a separate provision (section 4.C.) making clear that the *Memphis* clause does *not* apply either to the rates fixed by contract through the auction process, or to the agreed-upon transition payments. The settlement instead confirms that these contracted-for-rates cannot be modified unless changes are necessary in the public interest. The express purpose of section 4.C. is to "reduce regulatory uncertainty" by reassuring

market participants that the fixed-rate contracts contemplated under the settlement will be respected by the Commission. JA. 60-61.

The settlement's provisions are consistent with the Federal Power Act's requirements and this Court's precedents. As petitioners explain, this Court has long held that the statutory regime permits wholesale energy rates to be established by contract and protects the integrity of private contractual arrangements. *See* Pet. Br. 3–8. The *Mobile-Sierra* doctrine, named after this Court's landmark decisions, mandates that when wholesale energy rates are fixed by contract, the Commission has no authority to modify them except in "extraordinary circumstances" when unequivocally "necessary in the public interest." *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332, 344 (1956); *FPC v. Sierra Pac. Power Co.*, 350 U.S. 348 (1956). This Court reaffirmed *Mobile-Sierra* just last year in *Morgan Stanley Capital Group Inc. v. Public Utility District No. 1 of Snohomish County*, 128 S. Ct. 2733 (2008), emphasizing that Congress "intended to reserve the Commission's contract-abrogation power" only for "those extraordinary circumstances where the public will be severely harmed." *Id.* at 2749.

In its orders below, the Commission approved the proposed settlement, concluding that it establishes an effective process for resolving "the deficiencies in New England's existing capacity market." Pet. App. 135a. In addition, the Commission found that the settlement appropriately recognizes that rates fixed by contract through the capacity auction, as well as

the rates paid during the transition period, are subject to the *Mobile-Sierra* doctrine. Pet. Br. 12–14, U.S. Br. 10–11. The Commission thus confirmed that any parties choosing to participate in the capacity auction can rely on the outcome of that process, assured that contracted-for rates will not be changed unless unequivocally necessary in the public interest.

The court of appeals affirmed the Commission's orders in every respect, except one—specifically, the D.C. Circuit held that the Commission could not "approve a settlement agreement that applies" *Mobile-Sierra*'s "highly-deferential 'public interest' standard to rate challenges brought by non-contracting third parties." Pet. App. 21a. In reaching its decision, the lower court radically departed from this Court's precedents, recasting *Mobile-Sierra* as a narrow exception to the Federal Power Act's just-and-reasonable standard. *Id.* at 24a. The court of appeals held that "when a rate challenge is brought by a non-contracting third party, the *Mobile-Sierra* doctrine simply does not apply" and "the proper standard of review remains the 'just and reasonable' standard." *Id.* at 22a.

The decision below misunderstands the statutory requirements and is contrary to *Morgan Stanley*. By carving out a novel exception for rate challenges brought by non-contracting third parties, the D.C. Circuit has altered *Mobile-Sierra*'s balanced, even-handed public-interest standard on which thousands of wholesale power contracts are premised. If allowed to stand, the decision will subvert the long-settled expectations of market participants. It also will risk destabilizing the

Nation's energy markets, exposing consumers to the same types of high and volatile prices and supply shortages that prompted Congress to impose strict limits on the Commission's authority to undo private contractual arrangements.

This brief provides *amici*'s perspectives on the important issues raised in this case. First, the brief explains why the D.C. Circuit's newly minted third-party exception to *Mobile-Sierra* is contrary to this Court's precedents and, if allowed to stand, will eviscerate the *Mobile-Sierra* doctrine, produce an improper asymmetrical standard that favors buyers over sellers, and destabilize the Nation's energy markets. Second, the brief addresses an issue that the Court need not reach, but on which respondents' briefing focused in the court below—namely, the extent to which settlement agreements are subject to *Mobile-Sierra*. Respondents contend that different rules apply when parties proceed by settlement. In fact, whether *Mobile-Sierra* applies turns not on the label of the parties' agreement, but instead on whether the parties have fixed a rate by contract, even if the resulting contract is the product of a settlement. Third, the brief addresses the Commission's contention that its orders approving the parties' settlement are entitled to *Chevron* deference. The contracts resulting from the auction process constitute binding commitments to buy and sell capacity at fixed rates and, therefore, are subject to *Mobile-Sierra* as a matter of law. Because the Commission must comply with the statutory requirements, the Court need not address the scope of the Commission's

discretion in circumstances where rates are not fixed by voluntary agreement.

ARGUMENT

I. The Decision Below Contravenes This Court's Precedents And Misapplies The Statutory Requirements.

This Court has long held that when buyers and sellers establish rates by contract, the resulting rates are presumptively just and reasonable, and the Commission has no authority to modify them except in "extraordinary circumstances where the public will be severely harmed." *Morgan Stanley*, 128 S. Ct. at 2749. The decision below carves out a large, novel, and destabilizing exception to this constraint on the Commission's authority, concluding that rates are not presumptively just and reasonable when they are challenged by a non-contracting third party. The D.C. Circuit's decision is contrary to the express teachings of *Morgan Stanley* and, if left uncorrected, will effectively nullify the freedom of contract promoted by "decisions of this Court and the Court of Appeals" for "the past 50 years." *Id.* at 2739.

A. The D.C. Circuit's Decision Conflicts With *Morgan Stanley*.

The Federal Power Act provides that wholesale rates may be "established initially by contract," *Mobile*, 350 U.S. at 339, and the Court has clarified that, once rates are so established, the Commission has no authority to modify them, except in "extraordinary circumstances" when unequivocally "necessary in the public interest." *Id.* at 344;

Sierra, 350 U.S. at 348. As petitioners explain, this constraint on the Commission's authority, referred to as "the *Mobile-Sierra* doctrine," has played a central role in the development of the Nation's energy markets. *See* Pet. Br. 7–8; *see also* U.S. Br. 21–22.

Last Summer this Court affirmed *Mobile-Sierra*'s continuing vitality in *Morgan Stanley*. Reversing Ninth Circuit decisions that threatened "disfigurement of the venerable" doctrine, 128 S. Ct. at 2747, the Court reiterated that a "rate set out in a freely negotiated wholesale-energy contract" is presumed to satisfy "the 'just and reasonable' requirement imposed by law." *Id.* at 2737. The Court emphasized that "uncertainties regarding rate stability and contract sanctity can have a chilling effect on investments and a seller's willingness to enter into long-term contracts," which "in the long run" will "harm consumers." *Id.* at 2749. Accordingly, because the "regulatory system created" by the Federal Power Act is "premised on contractual agreements voluntarily devised by the regulated companies[,] it contemplates abrogation of these agreements only in circumstances of unequivocal public necessity." *Id.* at 2739 (quoting *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 822 (1968)).

Morgan Stanley should have prompted the D.C. Circuit to reconsider its decision below and to grant rehearing. *See* Pet. Br. 16–17; U.S. Br. 13. Instead, the D.C. Circuit left in place its initial decision (issued before *Morgan Stanley*), which characterized *Mobile-Sierra* as a narrow "exception" to the statutory requirement that rates

be "just and reasonable." The D.C. Circuit held that *Mobile-Sierra* "does *not* apply" when a "rate challenge is brought by a non-contracting third party." Pet. App. 22a (emphasis added). In the D.C. Circuit's view, applying *Mobile-Sierra* to challenges brought by non-contracting third parties would deprive those parties of their "statutory right to have rate challenges adjudicated under the 'just and reasonable' standard." *Id.* at 22a.

That reasoning is deeply flawed. *See* Pet. Br. 24–26; U.S. Br. 25–28. In *Morgan Stanley*, this Court went to great lengths to emphasize that it was not relying on the "obviously indefensible proposition that a standard different from the statutory just-and-reasonable standard applies to contract rates." *Morgan Stanley*, 128 S. Ct. at 2740. Contrary to the conclusions reached by the court below, the *Mobile-Sierra* doctrine is not only about ensuring that parties to a contract are held to their "contractual obligations." Pet. App. 24a. Instead, the doctrine recognizes the importance of contract integrity to the efficient working of the energy industry, and is premised on the notion that, because wholesale energy contracts are typically negotiated between sophisticated entities enjoying equal bargaining power, the contractually agreed-upon rate is expected to be, and by definition is, a "just and reasonable" rate. *Morgan Stanley*, 128 S. Ct. at 2746 (citing *Verizon Commc'ns, Inc. v. FCC*, 535 U.S. 467, 479 (2002)). The contracting process thus produces a rate that is "just and reasonable" both as between the contracting parties and as applied to everyone else. The *Mobile-Sierra* doctrine is not, as the D.C.

Circuit assumed, a narrow "exception" to the just-and-reasonable standard; instead, it is a "definition of what it means for a rate to satisfy" that standard when the rate is fixed by contract. *Id.*

Nor does applying the *Mobile-Sierra* doctrine deprive any party of its statutory rights. The Federal Power Act's "just and reasonable" standard is properly viewed not as a right bestowed upon regulated parties, but as a constraint that frames the boundaries of Commission action. *See* Pet. Br. 27. The *Mobile-Sierra* doctrine protects the integrity of privately negotiated agreements by denying the Commission authority to look beyond the general public interest to individual interests and agendas. The statutory limits on the Commission's authority do not change merely because a contract is challenged by a non-contracting third party.

B. The D.C. Circuit's Decision Eviscerates *Mobile-Sierra*.

If allowed to stand, the D.C. Circuit's newly minted third-party exception will eviscerate the *Mobile-Sierra* doctrine, and consign this Court's *Morgan Stanley* decision to a mere footnote in the regulation of the energy industry. As a practical matter, a third-party exception to *Mobile-Sierra* ensures that virtually no wholesale energy contract is protected from abrogation.

In contrast to standing requirements that apply to disputes over ordinary commercial contracts, *cf. Miree v. DeKalb County, Ga.*, 433 U.S. 25 (1977) (state law applies to determine whether third party beneficiaries enjoy standing), the

Federal Power Act confers standing on extraordinarily permissive terms. The statute allows virtually anyone to file a complaint with the Commission challenging an energy contract as unjust, unreasonable, or unduly discriminatory. *See* 16 U.S.C. § 825e (2006) ("[a]ny person ... complaining of anything done ... by any ... public utility ... may apply to the Commission by petition"). As the Commission's regulations state, "[a]ny person may file a complaint seeking Commission action against any other person alleged to be in contravention or violation of any statute, rule, order, or other law administered by the Commission, or for any other alleged wrong over which the Commission may have jurisdiction." 18 C.F.R. § 385.206(a) (2009).

The upshot is that non-contracting third parties can, and routinely do, file complaints with the Commission seeking to re-write energy contracts on grounds that the rates are either too high or too low. For example, in 2007, the Illinois Attorney General filed a complaint seeking to abrogate freely negotiated contracts between Illinois utilities and 16 wholesale suppliers that she alleged would lead to excessive charges on Illinois consumers. *See Amended Complaint by the People of the State of Illinois, ex rel. Illinois Attorney General Lisa Madigan*, FERC Dkt. No. EL07-47-000 (Mar. 16, 2007). Similarly, a consumer group filed complaints challenging a series of freely negotiated contracts between utilities and energy suppliers in California. *See* Section 206 Compl., FERC Dkt. No. EL07-50-000 (Mar. 26, 2007) (challenging contract between Southern California

Edison Co. and Blythe Energy, LLC); Section 206 Compl., FERC Dkt. No. EL07-40-000 (Mar. 2, 2007) (challenging contract between Pacific Gas & Electric Co. and Metcalf Energy Center, LLC and Los Medanos Energy Center, LLC); Section 206 Compl., FERC Dkt. No. EL07-37-000 (Feb. 22, 2007) (challenging contract between Southern California Edison Co. and Long Beach Generation, LLC).

Because long-term wholesale energy contracts are of concern not only to the parties who negotiate them but also to numerous third parties, there is no shortage of state regulators, consumer advocacy groups, retail consumers, industrial buyers, upstream suppliers, and other interested stakeholders willing to take advantage of the Federal Power Act's permissive standing requirements. In fact, as a practical matter, there will always be some non-contracting third party whose interests align with a buyer faced with contract rates that, in hindsight, appear too high. For this reason, allowing non-contracting parties to circumvent *Mobile-Sierra* would just as surely undermine "contract stability *as between the contracting parties*," Pet. App. 24a (emphasis in original), as would permitting a party to complain about contract rates to which it voluntarily agreed. When a contract rate becomes unfavorable due to unforeseen changes in market conditions or for any other reason, it is hard to fathom that any but the most noble or ignorant contracting parties would not seek to circumvent *Mobile-Sierra* by encouraging non-contracting parties to file

complaints challenging the contract as unjust and unreasonable.

This concern is highlighted in *Morgan Stanley*'s companion cases, which were vacated and remanded to the Ninth Circuit for further consideration. *See Sempra Generation v. Public Utils. Comm'n of Cal.*, 128 S. Ct. 2993 (2008). Because those cases involve public entities that were not original contracting parties, an issue raised in the companion cases not addressed in *Morgan Stanley* is the validity of the Commission's determination that the complainants, the California Public Utilities Commission and the California Electricity Oversight Board, had "stepped into the shoes" of the buyer under the challenged contracts. *See Public Utils. Comm'n of Cal. v. FERC*, 474 F.3d 587, 592 n.4 (9th Cir. 2006) (acknowledging this open issue). The Ninth Circuit has now remanded that issue to the Commission, *see Public Utils. Comm'n of Cal. v. FERC*, 550 F.3d 767 (9th Cir. 2008), and interested parties have submitted extensive briefing addressing whether *Mobile-Sierra* should apply. *See, e.g.*, Answer and Cross-Motion of Sempra Generation for Determination that the *Mobile-Sierra* Doctrine Applies to the California Public Utilities Commission, FERC Dkt. Nos. EL02-60-003, *et al.* (Dec. 19, 2008). Most relevant here, the complaining state agencies have argued that, in adjudicating their challenge to the contract rates, the Commission is not constrained by *Mobile-Sierra* because a different California agency signed the contracts and, therefore, the complainants qualify as "third parties" entitled to attack the contracts

under a *de novo* standard of review. *See* Answer of the Public Utilities Commission of the State of California to Cross Motion of Sempra Generation and Cross Motion for Summary Disposition, FERC Dkt. Nos. EL02-6-003, *et al.*, at 4–6 (Jan. 21, 2009) (citing the D.C. Circuit's *Maine PUC* decision and arguing that *Mobile-Sierra* does not apply); *see also* Answer and Cross-Motion of the Public Utilities Commission of the State of California for an Order Governing Procedures on Remand, FERC Dkt. Nos. EL02-60-003, *et al.*, at 22-26 (Jan. 14, 2009).

Indeed, in *Morgan Stanley* itself, numerous third parties stood ready to challenge the parties' contracts as imposing an "excessive burden" on third-party consumers. *See, e.g., Morgan Stanley v. Public Util. Dist. No. 1 of Snohomish County*, Nos. 06-1457 & 06-1462, Br. of AARP in Support of Respondents (Jan. 14, 2008); *id.*, Br. of Public Util. Law Project of New York, Inc. in Support of Affirmance (Jan. 16, 2008); *id.*, Br. of Colorado Office of Consumer Counsel, *et al.* in Support of Affirmance (Jan. 14, 2008). Recognizing the important role that contract sanctity has played in the development of the Nation's energy markets, this Court rejected the view that *Mobile-Sierra* does not apply when contract rates arguably impose an "excessive burden" on consumers. *Morgan Stanley*, 128 S. Ct. at 2747-48. That ruling will be largely meaningless if the Commission is exempt from *Mobile-Sierra* and the respect for contracts the Federal Power Act demands merely because a complaint is filed by a non-contracting third party.

C. The D.C. Circuit's Decision Will Produce An Asymmetrical Standard.

Recognizing that the universe of third-party complainants is potentially boundless, the Commission has suggested that, if the D.C. Circuit's policy innovations are allowed to stand, the Commission will police rate challenges brought by third parties to prevent "inappropriate strategic behavior." U.S. Cert. Opp. 12. That is another reason to reverse the court of appeals. Any attempt to distinguish *bona fide* third parties from complainants acting as impermissible "proxies" for contracting parties, *id.*, will inevitably produce an asymmetrical standard that favors buyers over sellers.

In wholesale energy markets, load serving entities, such as utilities and power marketers that serve retail customers (*i.e.*, "load"), will typically be net buyers of power—that is, they purchase power to serve customers above and beyond the power generated by their own units. Accordingly, when a load serving entity enters into a contract with rates that, in hindsight, may appear to be "too high," there will be no shortage of non-contracting third parties (such as state regulators, consumer advocacy groups, and retail customers) clamoring for relief at the Commission. Because the challenged contracts undoubtedly will have some effect on the rates paid by the load serving entity's customers, the Commission will find it difficult to sort out which customers are "prox[ies]" engaged in "inappropriate strategic behavior." *Id.* Likewise, because the Federal Power Act has "special solicitude for states and state agencies," *Maryland*

People's Counsel v. FERC, 760 F.2d 318, 320 (D.C. Cir. 1985) (Scalia, J.), the Commission will be hard pressed to characterize a state agency complainant as a "proxy" for the load serving entity, except in the unusual case where the load serving entity is also a state agency in the same State. *Cf. Public Utils. Comm'n of Cal. v. Sellers of Long Term Contracts*, 105 FERC ¶ 61,182 at P 51 (2003).

In contrast, independent power producers, like many of *amici*'s members, will almost always be net sellers of energy. If an independent power producer agrees to what, in hindsight, turns out to be an unfavorable deal, with rates that appear "too low," the consequences will fall first upon the power producer and its shareholders and then, in the unusual case, upon its lenders. To the extent any non-contracting third party challenges the contract rates, that party will likely be a shareholder or lender. But a shareholder or lender is precisely the type of complainant that might easily be viewed as a "proxy for one of the contracting parties." U.S. Cert. Opp. 12.

In other words, even if the Commission had discretion to mitigate the pernicious effects of the D.C. Circuit's new third-party exception, its attempts to do so will turn the even-handed *Mobile-Sierra* doctrine into a one-way ratchet that favors buyers over sellers. *See Morgan Stanley*, 128 S. Ct. at 2747 (recognizing that standard for buyer challenges "must be the same" as standard for seller challenges). Such a result is fundamentally at odds with *Mobile-Sierra*'s reliance on arms-length contracting, which in no way depends on whether the contract rate turns out to be "too high"

or "too low" in light of subsequent market developments. Such a result also would upset the "balancing of [] investor and [] consumer interests" that informs the contract-focused ratemaking process under the Federal Power Act. *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944). When Congress enacted the Federal Power Act, it "was not only expressing its conviction that the public interest requires the protection of consumers from excessive prices," but also "manifesting its concern for the legitimate interests of ... companies in whose financial stability the ... consuming public has a vital stake." *United Gas Pipe Line Co. v. Memphis Light, Gas & Water Div.*, 358 U.S. 103, 113 (1958).

D. The D.C. Circuit's Decision Will Inject Uncertainty Into The Nation's Energy Markets.

If allowed to stand, the D.C. Circuit's third-party exception to *Mobile-Sierra* will upend the stability of long-term contracts on which the Nation's energy markets depend. *See* Pet. Br. 40–41. In fact, because almost any contract could be challenged by a non-contracting third party, the D.C. Circuit's decision threatens to expose consumers to the very types of high prices and frequent supply shortages the Federal Power Act was designed to prevent.

It is hard to overstate the importance of regulatory certainty and contractual integrity to the efficient working of the energy industry. As this Court has recognized, contract stability is crucial because investors are loath to invest in

highly volatile power markets unless they can rely on the sanctity of fixed-price contracts. *See Morgan Stanley*, 128 S. Ct. at 2749; CERA Advisory Services, *California Power Crisis Aftershock: The Potential Modification of Western Power Contracts*, at 4–7 (Apr. 2007) ("*Aftershock*"); The Electric Energy Market Competition Task Force, *Report to Congress on Competition in Wholesale and Retail Markets for Electric Energy*, at 4 (Apr. 2007). Energy suppliers, like other market participants, "require clear signals regarding national policies and confidence that those policies will be sustained over time in order to undertake the substantial investment needed to support expected increases in consumption." Statement of Jim Wells, Director Natural Res. & Env't, GAO, Meeting Energy Demand in the 21st Century, GAO-05-414T, at 8 (Mar. 16, 2005). These important supply signals will be scrambled if contract rates are subject to change at the request of non-contracting third parties.

From an investor's perspective, it makes no difference whether a contract is subject to challenge by a disgruntled contracting party or by a "non-contracting third party." In either instance, investors will discount the value of contracts if there is a material risk that the Commission may later abrogate them. Sophisticated investors "will not participate in a market in which" non-contracting parties are allowed to undo contracts, "at least not without charging a significant risk premium—a cost that will ultimately be borne by consumers." *Standard of Review for Proposed Changes to Market-Based Rate Contracts for*

Wholesale Sales of Elec. Energy by Pub. Utils., Proposed Policy Statement, 100 FERC ¶ 61,145 at 61,545 (P 3) (2002) (Brownell and Breathitt, Comm'rs, concurring).

II. The Decision Below Rests On A Fundamental Misunderstanding Of The Statutory Requirements.

In carving out a novel third-party exception to *Mobile-Sierra*, the D.C. Circuit lapsed into error by accepting respondents' assertions that a settlement should not be permitted to "thrust" a "public interest" standard on non-contracting third parties. Pet. App. 22a. As petitioners emphasize, because the lower court's new third-party exception is improper and contrary to precedent, the Court should reverse without addressing the precise contours of when or to what extent a settlement may be protected under *Mobile-Sierra*. *See* Pet. Br. 20. If the Court does address the issue, however, it should recognize that whether *Mobile-Sierra* applies turns not on whether the parties are proceeding by settlement, but instead on whether the parties have fixed a rate by contract (even if the contract is the product of a settlement). It is the substance, not the label, of an agreement that determines whether it constitutes a fixed-rate contract protected from modification under the Federal Power Act.

A. *Mobile-Sierra* Applies To Rates Fixed By Contract.

The Federal Power Act contemplates two mechanisms for setting rates in the wholesale energy industry: either (i) by contract, or

(ii) unilaterally through *ex parte* filings. *See Mobile*, 350 U.S. at 343. Whether the *Mobile-Sierra* doctrine applies depends not on the identity of the party challenging the rate but on which mechanism is used to set the rate.

To ensure a stable and sufficient supply of affordable energy, Congress "rejected a pervasive regulatory scheme ... in favor of voluntary commercial agreements." *Otter Tail Power Co. v. United States*, 410 U.S. 366, 374 (1973); *see also Sunray Mid-Continent Oil Co. v. FPC*, 364 U.S. 137, 154 (1960). When buyers and sellers fix rates by contract, the rates are presumed to satisfy "the 'just and reasonable' requirement imposed by law." *Morgan Stanley*, 128 S. Ct. at 2737. In such circumstances, "the party charging the rate and the party charged [are] often sophisticated businesses enjoying presumptively equal bargaining power" who can be "expected to negotiate a 'just and reasonable' rate as between the two of them." *Id.* at 2746 (citing *Verizon*, 535 U.S. at 479). Accordingly, the *Mobile-Sierra* doctrine applies and the parties' contract may not be modified unless the Commission "concludes that the contract seriously harms the public interest." *Id.* at 2737.

In contrast, the *Mobile-Sierra* doctrine does not apply when rates offered to prospective customers are established unilaterally through *ex parte* filings. *See id.* at 2746 n.3 (the "public interest" is "relevant" but not the "sole concern" when rates are set unilaterally) (citing *Sierra*, 350 U.S. at 355). The Federal Power Act provides that, in the "absence of any contractual relationship, rates determined *ex parte* by the seller may be filed"

with, and allowed to become effective by, the Commission. *Memphis*, 358 U.S. at 112 (unless "it has undertaken by contract not to do so," a seller "has the right ... to change its rates ... [at] will"). Because a unilateral rate filing is not a contract, the rate schedule included in a generally applicable tariff on file with the Commission is merely an *offer* that a customer may accept either by taking service in accordance with the tariff's terms or by executing a service agreement with the seller. *See Metro East Ctr. for Conditioning & Health v. Qwest Comms. Int'l, Inc.*, 294 F.3d 924, 926 (7th Cir. 2002) (a "tariff is an offer that the customer accepts by using the product"); *see also* 18 C.F.R. § 35.2(b) n.1 (2009) (defining "tariff"). Similarly, market rules contained in a generally applicable tariff establish the means by which offers may be made and accepted by the Commission. *See* Pet. Br. 47–52. In either scenario, the tariff provisions are established unilaterally and, therefore, the Commission's authority to modify the tariff is not limited to instances of unequivocal public necessity.

In addition, because the Federal Power Act respects the integrity of privately negotiated agreements, the Court has held that parties may opt out of *Mobile-Sierra* by including in their contracts what is known as a *Memphis* clause. *Memphis*, 358 U.S. at 113. When parties include a *Memphis* clause in their agreement, they retain the right to make future unilateral filings with the Commission and the contract may be modified even if changes are not required in the public interest. *See id.* at 115 n.8. As this Court has recognized, parties retain "broad authority to specify whether"

the Commission may "review a contract rate solely for whether it violates the public interest or also for whether it results in an unfair rate of return." *Morgan Stanley*, 128 S. Ct. at 2739.

Viewed against this backdrop, the fact that a contract rate is the product of a negotiated settlement does not (and should not) make any difference for purposes of applying the *Mobile-Sierra* doctrine. It is the substance, not the label, of the agreement that matters.

When a settlement involves, or results in, a fixed-rate contract, the contract is subject to *Mobile-Sierra* unless the parties specify a different level of Commission review. For example, to the extent a public utility and its customer resolve rate litigation through a settlement agreement that fixes a specific rate (or rate formula) for sales to that customer, the settlement agreement itself constitutes a fixed-rate contract subject to *Mobile-Sierra*, unless the parties have agreed otherwise. Similarly, merely because market rules are established through a Commission-approved settlement does not exempt contracts formed pursuant to those rules from the *Mobile-Sierra* doctrine. In short, the fact that a fixed-rate contract may flow from, or is embodied in, a settlement of a prior dispute does not change its essential character. *See* Pet. Br. 47.

In contrast, to the extent a settlement addresses only terms and conditions of service in a unilateral tariff of general applicability, the fact that a dispute is resolved by agreement does not transform the generally applicable tariff provisions

into a fixed-rate contract. In this context, when market rules are agreed upon by regulated parties and approved by the Commission, the rules can be prospectively changed and the Commission's authority is not constrained. In such circumstances, the settlement does not fix by contract the rate agreed upon with any particular customer; instead, it merely establishes (for example) either the terms of offers made through the tariff, or the process for the submission and acceptance of offers through organized markets.

This is not to say that the policies underlying *Mobile-Sierra* are irrelevant when a settlement involves only a unilateral tariff of general applicability. *See* U.S. Br. 36–37. Courts have recognized that, even in instances where the *Mobile-Sierra* doctrine does not apply directly, the "*policies* articulated in *Mobile* and *Sierra* support treating a settlement agreement as a factual difference that may justify a rate disparity" without running afoul of the Federal Power Act's prohibition against undue discrimination. *Cities of Bethany v. FERC*, 727 F.2d 1131, 1139 (D.C. Cir. 1984) (emphasis added); *see also Town of Norwood v. FERC*, 202 F.3d 392, 402 (1st Cir. 2000) ("public interest in promoting settlements" may justify disparate treatment); *Cities of Newark v. FERC*, 763 F.2d 533, 546 (3d Cir. 1985) (discussing "strong policy arguments favoring settlement agreements"). In other words, even if a settlement does not embody a fixed-rate contract, the policy considerations that inform *Mobile-Sierra* may still be relevant in assessing whether the terms of a settlement should or should not be modified.

None of this, however, changes the basic rule: When parties agree to a contract rate—regardless whether the contract is reflected in a written or oral contract, a settlement, or some other expression of agreement—the contract is subject to the *Mobile-Sierra* doctrine and the Commission may not modify the contract except as necessary in the public interest.

B. *Mobile-Sierra* Applies To The Contract Rates At Issue In This Case.

When one focuses on the difference between unilateral *ex parte* filings and fixed-rate contracts, it is clear that there is no basis for crafting a novel third-party exception to *Mobile-Sierra*. The Commission properly approved the parties' proposed settlement, including the provisions recognizing that *Mobile-Sierra* applies to rates fixed by contract.

To be sure, the settlement provisions establishing new market rules for New England are not themselves fixed-rate contracts. The settling parties acknowledged as much by including a *Memphis* clause in their agreement. But that does not mean that the contract rates embodied in, and contemplated under, the proposed settlement—specifically, (i) the transition payments, and (ii) the rates resulting from the auction process—are not subject to the *Mobile-Sierra* doctrine. Because in both instances the rates are established by contract, they cannot be modified by the Commission unless modifications are necessary in the public interest.

This point is especially clear with respect to the rates established through the capacity auction. *See* Pet. Br. 47–52. The settlement's section 4.C. states that, although the rules for conducting the capacity auction are subject to modification by the Commission, once those rules are approved and in place, the rates fixed in contracts resulting from the capacity auction will be subject to *Mobile-Sierra*. *See* U.S. Br. 10. The D.C. Circuit accepted respondents' assertions that this provision was somehow "thrusting" *Mobile-Sierra* on non-contracting third parties. In fact, the provision merely restates what the law already requires.

Section 4.C. was appropriately included in the settlement because it clarifies that the generally applicable tariff filed by ISO New England Inc. should not be construed to lift the ordinary *Mobile-Sierra* protections for rates fixed by contract. When a regional transmission organization ("RTO") or independent transmission operator ("ISO"), files a unilateral tariff offering rates to prospective electric transmission customers, the tariff contains detailed rules for the organized markets administered by the RTO or ISO. Among other things, these rules set forth an offer-and-acceptance process through which parties may enter binding fixed-rate contracts without reducing their agreements to writing. Significantly, however, it is not unusual for these sorts of tariffs to include a *Memphis* clause. *See, e.g., Pro Forma Open Access Transmission Tariff*, § 9, Original Sheet No. 37; *see also* ISO New England Inc., FERC Electric Tariff No. 3, § I.8, First Revised Sheet No. 27. That unilaterally imposed provision preserves the RTO's

or ISO's right to seek prospective changes to the tariff.

Although section 18 of the ISO New England tariff includes a provision that could be construed to be a *Memphis* clause, the settlement avoids confusion by making clear in section 4.C. that the provision does not apply to contracts resulting from the auction process. Section 4.C. thus serves to reassure market participants that the rates established through the capacity auction will be subject to the "default rule" of *Mobile-Sierra* and, therefore, treated the same as any other rates fixed by voluntary agreement. *Morgan Stanley*, 128 S. Ct. at 2739. Far from thrusting a unilateral standard on non-contracting parties, the settlement confirms that the Federal Power Act's ordinary requirements will apply.

More broadly, the D.C. Circuit's decision fundamentally misconstrues the *Mobile-Sierra* doctrine. Putting to one side the complexities of the settlement, the decision below appears premised on a notion that when parties agree to a contract rate, they are somehow disadvantaging non-contracting third parties by "thrusting" a more stringent standard of review on would-be challengers. But *Mobile-Sierra* recognizes that agreed-on rates that are the product of arms-length contracting are presumptively just and reasonable. The resulting standard of review flows ineluctably from that legal and regulatory framework and is not a disadvantage that is thrust upon non-contracting parties. Although such a presumptively reasonable rate may make it harder for third parties to challenge the rate, it no more

disadvantages third parties than reasonable government action disadvantages parties who could otherwise complain that the action is arbitrary and capricious.

III. This Court Should Reject The Commission's Attempt To Loosen The Statutory Constraints On Its Authority.

In opposing the petition for *certiorari*, the Commission soothingly suggested that it could "mitigate" the pernicious effects of the D.C. Circuit's third-party exception by rejecting "rate challenges that amount to inappropriate strategic behavior, such as a third-party complaint challenging a contract filed by a 'proxy' for one of the contracting parties." FERC Opp. 11-12. In its merits brief, the Commission tacks in a different direction, acknowledging that the D.C. Circuit's third-party exception is improper, but arguing that the Commission is entitled to *Chevron* deference in determining when the *Mobile-Sierra* doctrine should apply. *See* U.S. Br. 24–25, 30-33 (citing *Chevron U.S.A., Inc. v. NRDC*, 467 U.S. 837 (1984)).

The Commission took a similar approach in *Morgan Stanley*, contending that its decision to apply *Mobile-Sierra* to the contracts in that case deserved *Chevron* deference. *See Morgan Stanley*, 128 S. Ct. at 2745. The Court rejected that contention. Because the contracts in *Morgan Stanley* were fixed-rate contracts, "the Commission was *required* ... to apply the *Mobile-Sierra* presumption in its evaluation of the contracts here." *Id.* (emphasis in original). The Court did not, however, opine more broadly on whether there

may be other circumstances in which the Commission is entitled to *Chevron* deference. The Court should take a similar approach here.

In its brief on the merits, the Commission attempts to avoid the statutory constraints on its authority by arguing that the "results of the capacity auctions, although possessing certain characteristics of contracts, do not constitute contracts between buyers and sellers." U.S. Br. 30. But the Commission cites *no precedent* supporting this startling proposition. It merely asserts that, although the capacity auction produces binding commitments to sell and purchase capacity, *see* Pet. Br. 10, the resulting agreements are not subject to *Mobile-Sierra* because they "are not recorded" in "separate" written documents and because the consequences of default are described in the tariff. U.S. Br. 30.

The notion that only separate, fully integrated written agreements are subject to *Mobile-Sierra* has long been rejected. Almost 35 years ago, the D.C. Circuit held that the *Mobile-Sierra* doctrine applies to unwritten contracts because the Commission has an obligation "to respect contractual obligations of whatever nature" when those contracts serve the purpose of fixing rates. *Sam Rayburn Dam Elec. Coop. v. FPC*, 515 F.2d 998, 1008-1009 (D.C. Cir. 1975). As petitioners correctly explain, the sales occurring through auction are contracts because they result from a voluntary contracting process that fixes the rate at which capacity is sold and purchased. *See* Pet. Br. 47-48 (citing precedent). Moreover, although contracts resulting from the capacity auction may

incorporate general terms and conditions from the tariff (just as private contracts may incorporate the Uniform Commercial Code or Commercial Arbitration Rules), the critical price and quantity terms are not incorporated from, or reflected in, the tariff. Instead, price and quantity are determined through the auction process itself and, under the settlement, are reflected in separate filings made with the Commission under section 205 of the Federal Power Act—the same statutory provision under which contracts, unilateral tariffs, and other rate schedules are traditionally filed. *See* ISO New England Inc., FERC Electric Tariff No. 3, § III.13.8.2, First Revised Sheet No. 7319L (requiring the ISO to file information, including the prices set through the auction process, a list of which resources received capacity supply obligations, and the amount of those obligations); *see also* J.A. 118 (same). Accordingly, precisely because the rates resulting from the capacity auction represent binding obligations fixed by voluntary agreement between buyer and seller, the contracts rates are protected under the Federal Power Act and the Commission has no authority to modify them.

As courts have recognized, the Commission has demonstrated a long-standing ambivalence to, and sometimes even hostility towards, the *Mobile-Sierra* doctrine. *See, e.g., Boston Edison Co. v. FERC*, 233 F.3d 60, 68 (1st Cir. 2000) (the Commission is "becoming hostile to *Mobile-Sierra*"); *Rayburn*, 515 F.2d at 1005 (the Commission's "distaste for the *Mobile-Sierra* doctrine is well known"); *Borough of Lansdale v. FPC*, 494 F.2d

1104, 1110 (D.C. Cir. 1974) (same). This Court should therefore decline the Commission's invitation to loosen the statutory constraints on its authority. *Cf. Louisiana Pub. Serv. Comm'n v. FCC*, 476 U.S. 355, 374-75 (1986) (an "agency may not ... expand its power in the face of a congressional limitation on its jurisdiction"); David B. Spence & Frank Cross, *A Public Choice Case for the Administrative State*, 89 Geo. L.J. 97, 113 (2000) ("when an agency must make decisions about the reach of its own jurisdiction, self-interest propels the agency toward ever more expansive interpretations of the law"). Instead, to the extent it addresses the issue, the Court should reaffirm that, although the Commission is generally entitled to deference "in its rate decisions," *Morgan Stanley*, 128 S. Ct. at 2738, the Commission has no discretion to pick and choose which contracts are subject to the *Mobile-Sierra* doctrine.

This Court's decisions in *Mobile* and *Sierra*, as affirmed in *Morgan Stanley*, articulate a clear and binding interpretation of what the statutory language demands, recognizing that the statute imposes important constraints on agency decisionmaking by framing the boundaries of permissible Commission action. In particular, as described above, the Federal Power Act ensures that market participants can rely on the sanctity of long-term contracts by mandating that the Commission's interference with private contractual arrangements is limited. *See Public Serv. Comm'n of State of New York v. FERC*, 866 F.2d 487, 488-89 (D.C. Cir. 1989) (noting that courts have repeatedly "repelled" the Commission's "gambit" to

"compromise [the] limits ... on its power to revise rates"). Accordingly, because this Court has determined the Federal Power Act's clear meaning, it need not "reach any issue of deference" to the Commission. *Lechmere, Inc. v. NLRB*, 502 U.S. 527, 536 (1992).

Having "bargain[ed] in the shadow" of *Mobile-Sierra* for more than five decades, *Boston Edison*, 233 F.3d at 66, energy market participants have ordered their affairs on the assumption that the Commission is permitted to modify contracts only in accordance with *Mobile-Sierra*'s well-defined understanding of "extraordinary circumstances" of "unequivocal public necessity." *Permian*, 390 U.S. at 822. Upsetting those expectations not only engenders uncertainty, it invites an interlude of unpredictable agency reaction. The risk that market participants will be subject to uncertain Commission policies poses a further threat to the stability of our Nation's energy markets. That threat can and should be defused by this Court's reversal of the decision below.

CONCLUSION

For the foregoing reasons, the Court should reverse the judgment of the Court of Appeals.

Respectfully submitted,

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AMICUS CURIAE BRIEF

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IN THE

Supreme Court of the United States

NRG POWER MARKETING, LLC, *ET AL.*,

Petitioners,

v.

MAINE PUBLIC UTILITIES COMMISSION, *ET AL.*,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF MORGAN STANLEY CAPITAL GROUP INC., THE INTERNATIONAL SWAPS AND DERIVATIVES ASSOCIATION, INC., AND THE FINANCIAL INSTITUTIONS ENERGY GROUP AS *AMICI CURIAE* IN SUPPORT OF PETITIONERS

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BRIEF OF MORGAN STANLEY CAPITAL GROUP INC., THE INTERNATIONAL SWAPS AND DERIVATIVES ASSOCIATION, INC., AND THE FINANCIAL INSTITUTIONS ENERGY GROUP AS *AMICI CURIAE* IN SUPPORT OF PETITIONERS

Morgan Stanley Capital Group Inc., the International Swaps and Derivatives Association, Inc., and the Financial Institutions Energy Group respectfully submit this brief as *amici curiae* in support of the petitioners.[1]

INTEREST OF *AMICI CURIAE*

Morgan Stanley Capital Group Inc. (Morgan Stanley), the commodities division of Morgan Stanley, is a "power marketer": an entity with regulatory approval from the Federal Energy Regulatory Commission (FERC or the Commission) to buy and sell, at market-based rates, wholesale electricity that it does not produce. Morgan Stanley was one of the first entities approved to sell power in this manner, having initially received its market-based authority in 1994 and then having repeatedly received authorization thereafter. *See Morgan Stanley Capital Group, Inc.*, 69 F.E.R.C. ¶ 61,175 (Nov. 8, 1994), *see also, e.g., Morgan Stanley Capital Group, Inc.*, No.

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[1] Pursuant to Rule 37.6, counsel for *amici curiae* state that no counsel for a party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person or entity other than *amici curiae*, their members, or their counsel has made a monetary contribution to the preparation or submission of this brief. The parties have filed letters of consent to the filing of this brief. Letters reflecting such consent have been filed with the Clerk.

ER94-1384-029 (June 26, 2001) (application filed November 8, 2000).

The International Swaps and Derivatives Association, Inc. (ISDA), which represents participants in the privately negotiated derivatives industry, is the largest global financial trade association by number of member firms. ISDA was chartered in 1985 and today has over 825 member institutions from 57 countries on six continents. These members include most of the world's major institutions that deal in privately negotiated derivatives, as well as many of the businesses, governmental entities and other end users that rely on over-the-counter derivatives to manage efficiently the risks inherent in their core economic activities. Since its inception, ISDA has pioneered efforts to identify and reduce the sources of risk in the derivatives and risk management business.

The Financial Institutions Energy Group (FIEG) is a group of banks and other financial institutions, all of which play a vital role in the electric utility industry. The businesses of FIEG members (and their affiliates) as they relate to the energy sector are very diverse. They are directly involved in the purchase and sale of electric energy, capacity, and ancillary services, and many, like Morgan Stanley, are power marketers with market-based rate authority. They are also involved in a wide array of other businesses that are only incidentally related to the electric industry. For example, FIEG members may act as market-making dealers, participants in physically and financially settled derivative transactions designed to hedge certain counterparty risk or to establish a proprietary position in the market, arrangers

of loan facilities, and underwriters of debt and equity securities.

Members of ISDA and FIEG are substantial participants in the market for wholesale electric power. Some members own interests in companies that produce electric power and sell it in the wholesale market. Some members own interests in retail distribution companies that purchase power in the wholesale market and distribute it to end users. Predominantly, however, members of these *amici*, like Morgan Stanley, operate as power marketers in the wholesale market; they contract with power producers, distribution companies, and other power marketers to buy or sell wholesale power that will ultimately be produced, resold, or distributed by others.

Power marketers like Morgan Stanley and the members of ISDA and FIEG play an extremely important role in wholesale power markets. Their expertise and extensive trading operations allow them to mitigate the financial risks that power manufacturers or distributors would otherwise have to incur in producing or distributing power. By assembling a diverse portfolio of contractual obligations to buy and sell power at different times and different prices, power marketers can insulate themselves from many of the risks of temporary price volatility, which are inherent in the energy market, as well as longer term unfavorable price trends. By contracting with producers and distributors of power, these marketers also allow producers and distributors to avoid those risks.

Unlike power producers, which generally participate in the energy market as sellers, and distribu-

tion companies, which participate as buyers, power marketers tend over the long term to be neither net sellers nor net purchasers of power. Consequently, they have no vested interest in rules that systematically favor either sellers or buyers. Their interest, instead, is in rules that ensure that the *market* operates effectively. They therefore are especially well suited to address the implications of the court of appeals' decision below for the effective functioning of the market for wholesale energy sales and purchases.

Both ISDA and FIEG accordingly participated as *amici curiae* in support of petitioners in *Morgan Stanley Capital Group Inc. v. Public Utility District No. 1 of Snohomish County*, 128 S. Ct. 2733 (2008). Morgan Stanley of course was a petitioner in that case. Morgan Stanley, ISDA, and FIEG now participate as *amici curiae* in this case principally to explain that, whereas the Court's recent decision two Terms ago in *Morgan Stanley* strongly reaffirmed the central role of contractual stability in securing the effective functioning of the market for wholesale power, an affirmance of the court of appeals in this case would essentially negate the decision in *Morgan Stanley* and the vital protection of contractual stability on which the decision is grounded.

INTRODUCTION AND SUMMARY OF ARGUMENT

Under the Federal Power Act (FPA), 16 U.S.C. §§ 791a *et seq.*, FERC possesses authority to regulate the transmission and sale of wholesale electricity. The FPA prescribes that all wholesale energy rates must be "just and reasonable," and any rate failing

to qualify as "just and reasonable" is "declared to be unlawful." 16 U.S.C. § 824d(a). The FPA grants FERC authority to review, on its own initiative or in response to a complaint, whether existing rates comply with the "just and reasonable" standard, and to determine and fix by order a "just and reasonable rate" upon concluding that an existing rate is "unjust, unreasonable, unduly discriminatory or preferential." 16 U.S.C. § 824e(a).

The degree of latitude possessed by FERC to modify an existing rate on the ground that it fails to qualify as "just and reasonable" varies depending on whether the rate was established unilaterally by tariff or instead by a negotiated contract. The *Mobile-Sierra* doctrine, *see United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332 (1956); *FPC v. Sierra Pac. Power Co.*, 350 U.S. 348 (1956), establishes a presumption that wholesale energy contracts negotiated by sophisticated parties produce just and reasonable rates. Contract rates, that is, presumptively *are* "just and reasonable," and may be set aside by FERC only in narrow situations in which their continued enforcement would "violate[] the public interest." *Morgan Stanley*, 128 S. Ct. at 2739. In the case of a rate established unilaterally by tariff, FERC retains greater latitude to set aside the rate as unjust and unreasonable "if it results in an unfair rate of return, not just if it violates the public interest." *Id.*

Those two forms of review—the more stringent public interest standard for contract rates and the "ordinary" just-and-reasonable standard for non-contract rates—each constitute applications to their distinct contexts of the FPA's overarching "just and

reasonable" standard. *Id.* at 2740. The *Mobile-Sierra* public-interest standard therefore "refers to the differing application of th[e] just-and-reasonable standard to contract rates." *Id.*

This Court strongly reaffirmed the vitality of the *Mobile-Sierra* presumption for contract rates in its decision two Terms ago in *Morgan Stanley*. In doing so, the Court emphasized "the important role of contracts in the FPA" and the FPA's "recogni[tion] that contract stability ultimately benefits consumers." *Id.* at 2749. Conversely, the Court explained, "uncertainties regarding rate stability and contract sanctity can have a chilling effect on investments and a seller's willingness to enter into long-term contracts and this, in turn, can harm customers in the long run." *Id.* (quoting Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities, 72 Fed. Reg. 39,904, 39,906–07 (July 20, 2007)).

The court of appeals below confined the *Mobile-Sierra* presumption to rate challenges brought by a contracting party, holding the "*Mobile-Sierra* doctrine simply does not apply" when "a rate challenge is brought by a non-contracting third party." Pet. App. 22a. That approach, if affirmed, would substantially undermine, if not completely destroy, the vital protection of contract stability secured by the recent reaffirmation of *Mobile-Sierra* in *Morgan Stanley*. The court of appeals' decision enables any affected third party to challenge and potentially invalidate any wholesale energy contract as "unjust and unreasonable" without regard to the "public interest" standard, thus allowing any third party to

seek to set aside a contract rate free from the presumption of validity demanded by *Mobile-Sierra*.

Indeed, the court of appeals' decision below affects the sanctity of the very contracts at issue in *Morgan Stanley* itself. One of the respondents in the *Morgan Stanley* case, the Nevada Bureau of Consumer Protection, has argued before FERC on remand from this Court's decision that, under the D.C. Circuit's decision below, it can freely challenge the rates in the *Morgan Stanley* contracts unencumbered by the *Mobile-Sierra* presumption. The Court's opinion in *Morgan Stanley*, however, nowhere suggests that the public interest standard it ordered the Commission to apply was applicable only to the contracting respondents. On the contrary, the Court emphasized that "[t]here is only one statutory standard for assessing wholesale electricity rates"—the just-and-reasonable standard—and when that standard is applied to contracted-for rates, it permits the Commission to overturn only rates that would "seriously harm the public interest." *Morgan Stanley*, 128 S. Ct. at 2745, 2747. The D.C. Circuit's decision varies the application of the statutory standard, to the very same rate, based on who asks FERC to apply it. There is no justification for applying a varied interpretation to the fixed terms of the statute in that manner.

Such an approach is particularly problematic in the context of the FPA. Contracts play an integral role in that statutory scheme, and contract stability is essential to the wholesale energy markets to which the statute applies. The uncertainty created by the court of appeals' approach would thoroughly undermine contractual integrity, with substantial

adverse implications for the effective functioning of those markets. In particular, the court of appeals' approach would (i) make it very difficult to attract sufficient capital to build and maintain the expansive (and expensive) infrastructure necessary to produce, transport, and deliver energy; (ii) encourage power marketers, who depend on the enforceability of their contracts to make a profit, to shift their capital to other markets with lesser levels of costs and risks; and (iii) discourage power sellers from entering into long-term agreements precisely when their capacity and price certainty are most needed by buyers. The result ultimately would be to harm the consumers that rely on the wholesale energy market for the power they use every day.

ARGUMENT

I. THE COURT OF APPEALS' NON-PARTY EXCEPTION TO *MOBILE-SIERRA* WOULD ESSENTIALLY NULLIFY THIS COURT'S DECISION MERELY TWO TERMS AGO IN *MORGAN STANLEY*

Two Terms ago, this Court in *Morgan Stanley* strongly reaffirmed its landmark decisions in *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332 (1956), and *FPC v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956), and the centrality of contractual integrity to the operation of the FPA. But that recent victory—for the petitioners in that case, for the effective functioning of wholesale energy markets, and ultimately for the consumers who rely on them—has been put substantially at risk by the court of appeals' decision below. The D.C. Circuit's decision cannot be reconciled with this Court's

precedent or with the terms of the FPA, which establish one—and only one—standard governing the review of rates established by contract, regardless of the identity of the party bringing a challenge.

A. *Morgan Stanley* Preserved and Reaffirmed the Centrality of Contract Stability under the Federal Power Act

Morgan Stanley arose out of a dispute involving, *inter alia*, a long-term wholesale power contract between Morgan Stanley and respondent Public Utility District No. 1 of Snohomish County Washington (Snohomish), during the 2000-2001 crisis in the energy markets in the Western States. Eventually, the prevailing market rates for short-term power fell below the rate established in Snohomish's contract with Morgan Stanley. Snohomish then filed a complaint with FERC, seeking to set aside the terms of its contract with Morgan Stanley. Other companies likewise challenged contracts they made during the crisis to purchase power. Certain non-contracting entities and individuals, including the Nevada Attorney General, Bureau of Consumer Protection (BCP), and a Senator from the State of Washington, sought to intervene before the Commission on the challengers' behalf. FERC rejected those challenges, emphasizing the importance of contract stability under the FPA. The Ninth Circuit reversed, holding that the *Mobile-Sierra* presumption was inapplicable in those circumstances for a number of reasons. *See Morgan Stanley*, 128 S. Ct. at 2743-45.

This Court largely reversed the decision of the Ninth Circuit. The Court began by reiterating that,

"[u]nder the *Mobile-Sierra* doctrine, [FERC] must presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law," and it may revise those rates only if they place "an excessive burden on consumers or otherwise seriously harm the public interest." *Id.* at 2737, 2750. The Court concluded that the Ninth Circuit had failed to abide by the *Mobile-Sierra* rule, and had given "short shrift to the important role of contracts in the FPA" in several respects. *Id.* at 2749.

First, by limiting application of *Mobile-Sierra* to instances in which FERC had pre-approved the market-based contract rates, the Ninth Circuit had erroneously "read *Sierra* as the equivalent of an estoppel doctrine" rather than "a definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context." *Id.* at 2746 (internal quotation marks omitted). Second, by limiting the application of *Mobile-Sierra* where there was a possibility of market dysfunction, the Ninth Circuit had "enabl[ed] sophisticated parties who weathered market turmoil by entering long-term contracts to renounce those contracts once the storm ha[d] passed," thus "reduc[ing] the incentive to conclude such contracts in the future" and "undermin[ing] the role of contracts in the FPA's statutory scheme." *Id.* at 2747. Third, by adopting a "zone of reasonableness" test to evaluate a buyer's challenge that rates are too high, the Ninth Circuit had failed "to accord an adequate level of protection to contracts." *Id.* at 2747, 2749. As this Court explained, "[a] presumption of validity that disappears when the rate is

above marginal cost is no presumption of validity at all." *Id.* at 2748.

Finally, the Court turned to two issues on which it concluded remand to the Commission was required: (i) whether the challenged agreements imposed an excessive burden on customers "down the line," and (ii) whether any party had engaged "in such extensive unlawful market manipulation" as to affect negotiation of the contract rates. 128 S. Ct. at 2747, 2749-51. The Court remanded the case for the Commission to "amplify or clarify" its findings on those two issues. *Id.*

B. The Decision Below Is Irreconcilable with *Morgan Stanley*

The Court's decision in *Morgan Stanley* reaffirms a long line of precedent in which this Court has recognized that Congress "built the regulatory system" of the National Gas Act and FPA "on a foundation of private contracts." *Sunray Mid-Continent Oil Co. v. FPC*, 364 U.S. 137, 154 (1960). The decision of the D.C. Circuit in this case puts that foundation, including the outcome in *Morgan Stanley* itself, at risk.

The court of appeals' "third-party exception" to the presumption of reasonableness would effectively swallow the *Mobile-Sierra* rule. By misreading *Mobile-Sierra* as "depart[ing] from the usual 'just and reasonable' standard," the court of appeals misunderstood the FPA to permit virtually anyone but a contracting party—including individual end consumers, corporations, governmental entities, and state regulators—to attack contractually negotiated rates as unjust and unreasonable without any pre-

sumption of validity. *See* Pet. App. 22a (explaining that "[i]t goes without saying that a contract cannot bind a nonparty") (internal quotation marks omitted). The decision thus eliminates any semblance of the contractual integrity that this Court has long recognized to be integral under the FPA. A contracting party desiring to set aside a negotiated rate without having to overcome the *Mobile-Sierra* presumption need only find some non-contracting party willing to take up the challenge.

Indeed, one of the respondents in the *Morgan Stanley* case itself has argued that the case should have been decided differently under the rule established by the court of appeals in this case. Several of the parties that opposed the contracts at issue in *Morgan Stanley* were non-parties to the agreements. *See, e.g., Nev. Power Co. v. Enron Power Mktg., Inc.*, 103 F.E.R.C. ¶ 61,353, at 62,388-89 (2003) (discussing Senator's request for rehearing); *Pub. Utils. Comm'n of Cal. v. Sellers of Long Term Contracts*, 99 F.E.R.C. ¶ 61,087, at 61,377, 61,382-83 (2002) (discussing complaints filed by the Public Utilities Commission of the State of California and the California Electricity Oversight Board), *reh'g denied*, 100 F.E.R.C. ¶ 61,098 (2002). One of those non-parties, the Office of the Nevada Attorney General, Bureau of Consumer Protection (Nevada BCP), was a respondent before this Court. *See Morgan Stanley*, 127 S. Ct. at 2736.

This Court's mandate in *Morgan Stanley* made plain that the Commission on remand was to apply the *Mobile-Sierra* public-interest standard to the

contracts at issue in the case.[2] The Nevada BCP nonetheless has argued on remand that the D.C. Circuit's opinion below "precludes application of the *Mobile-Sierra* presumption of justness and reasonableness in evaluating the Nevada BCP's challenge" to the very same contracts. Nevada Attorney General, Bureau of Consumer Protection Answer to Snohomish's Cross-Motion for Procedures on Remand of *Morgan Stanley* at 3-4 (Dec. 9, 2008) (Nevada BCP Answer). The BCP accordingly asserted that the Commission could, "based on its findings to date, conclude that the rates included in the . . . Nevada contracts [before the Commission] are unjust and unreasonable" and "order refunds" based on "the difference between the contract rates and just and reasonable rates." *Id.* at 4.

The Commission rejected Nevada's argument as "premature," and "strongly encourage[d] all parties in th[e] matter to settle their disputes." FERC Order on Remand at 15 n.63 & 18, No. EL02-28-006, et al. (Dec. 18, 2008). The BCP, however, filed a petition for rehearing, arguing that the paper hearing ordered by FERC "was unnecessary and inappropriate" in that the "Commission erred in failing to specify that, pursuant to *Maine PUC*, the *Mobile-Sierra* presumption of justness and reasonableness does not apply to the Nevada BCP's challenge to the NV Energy contracts at issue in [*Morgan Stanley*]." Re-

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[2] *See, e.g.*, *Morgan Stanley*, 128 S. Ct. at 2750 (Commission on remand to consider whether increase in rates during the crisis was "so great that, even taking into account the desirability of fostering market-stabilizing long-term contracts, the rates impose an excessive burden on consumers or otherwise seriously harm the public interest").

quest for Rehearing of the Office of the Nevada Attorney General, Bureau of Consumer Protection at 2, 7 (Jan. 20, 2009). FERC has yet to rule on the petition for rehearing.

The Nevada BCP's position in *Morgan Stanley* vividly illustrates the mischief that the decision below would enable. Contrary to the argument of the BCP and the decision of the court of appeals below, there is no basis for concluding that the justness and reasonableness of a contract rate could depend upon who is challenging it. As this Court emphasized in *Morgan Stanley*, "[t]here is only one statutory standard for assessing wholesale electricity rates," *i.e.*, "the just-and-reasonable standard." 128 S. Ct. at 2745. And there is only one "definition of what it means for a rate to satisfy the just-and-reasonable standard in the contract context": the public interest requirement of *Mobile-Sierra*. *Id.* That standard applies uniformly when assessing the validity of a contracted-for rate, "regardless of when the contract is reviewed," *id.*, and regardless of the identity of the party bringing a challenge.

II. THE COURT OF APPEALS' DECISION WILL HARM CONSUMERS BY IMPEDING THE EFFICIENT OPERATION OF THE WHOLESALE POWER MARKET

The *Mobile-Sierra* presumption rests on the intuition that markets generally cannot operate efficiently unless contracting parties have confidence that contractual commitments will be enforced. The need for contract stability is especially critical in the market for wholesale power, which requires clear, stable, and enforceable contract rights for its very

existence. Without that guarantee, the market (i) will not be able to attract sufficient capital to build and maintain the extensive and expensive infrastructure required for the production, transportation, and delivery of energy; (ii) will not be able to secure the participation of power marketers, who make the market more competitive; and (iii) will not be able to ensure that energy is provided to the public when the need for such power is at its greatest. A market operating under these constraints will fail to provide the service required by consumers who rely on it for their daily energy needs.

1. The contractual stability secured by *Mobile-Sierra* is critical to the wholesale power market, first and foremost, because the massive investments needed to build and maintain the infrastructure for the production, transportation, and delivery of power require that market participants have confidence that their agreements will remain binding in the future, even if one of the parties comes to conclude in hindsight that the original deal was improvident. As this Court recognized in *United Gas Pipe Line Co. v. Memphis Light, Gas & Water Division*, 358 U.S. 103 (1958), without reliable legal protection of energy producers' contract rights, "the maintenance and expansion of their systems through equity and debt financing would become most difficult, if not impossible." *Id.* at 113. Since the enactment of the FPA, "[e]conomies of scale have justified the construction of large . . . generation facilities" that produce power more efficiently and cheaply than ever before—but that also require ever-more significant amounts of capital to create. *Transmission Access Policy Study Group v. FERC*, 225 F.3d 667, 681 (D.C. Cir. 2000).

Contract stability is so important in the context of the energy markets that, in certain instances, FERC has "encourage[d] investment in new generation capacity by ensuring increased stability in . . . revenues, not [by adopting] higher rates across the board." *Elec. Consumers Res. Council v. FERC*, 407 F.3d 1232, 1237 (D.C. Cir. 2005). As FERC recognized when it ordered enforcement of the contracts in *Morgan Stanley*, "[c]ompetitive power markets simply cannot attract the capital needed to build adequate generating infrastructure without regulatory certainty, including certainty that the Commission will not modify market-based contracts unless there are *extraordinary* circumstances." *Nev. Power Co. v. Duke Energy Trading & Mktg. L.L.C.*, 99 F.E.R.C. ¶ 61,047, at 61,190 (2002).

Application of the *Mobile-Sierra* presumption affords that certainty. When the public interest standard is properly applied, litigation over long-term supply contracts is rare. *See Cities of Bethany v. FERC*, 727 F.2d 1131, 1139 (D.C. Cir. 1984) ("[F]ixed rate contracts . . . promote market stability and reduce litigation over rate filings."). Until the Ninth Circuit's opinion in *Morgan Stanley* (which, of course, this Court largely reversed) and the D.C. Circuit's opinion in this case, the breadth and continued vitality of this Court's landmark decisions in *Mobile* and *Sierra* had never been seriously threatened. *See Boston Edison Co. v. FERC*, 233 F.3d 60, 66 (1st Cir. 2000) (Boudin, J.) (noting that "the two cases are probably among the dozen best-known public utility decisions by the Supreme Court in this century"). Relying on this consistent precedent, contracting parties have understood that, as a matter of

practical reality, "[t]he obstacle that the public-interest standard presents to a rate change is almost insurmountable." *Kan. Cities v. FERC*, 723 F.2d 82, 87-88 (D.C. Cir. 1983) (Scalia, J.).

In contrast to the "refreshingly simple" *Mobile-Sierra* standard, *ASARCO, Inc. v. FERC*, 777 F.2d 764, 769 n.3 (D.C. Cir. 1985) (internal quotation marks omitted), the ordinary just-and-reasonable standard applicable to non-contract rates permits FERC to modify rates whenever they deviate from an ill-defined "zone of reasonableness." *See Permian Basin Area Rate Cases*, 390 U.S. 747, 767 (1968). And, if affirmed, the court of appeals' approach would cause even more uncertainty—not only because it would freely permit avoidance of the *Mobile-Sierra* presumption when a non-party asserts a challenge, but also because it will require litigation over questions such as whether a non-party is really a "proxy for one of the contracting parties" such that *Mobile-Sierra* would nonetheless apply. *See* Br. for the FERC, *NRG Power Mktg., LLC v. Me. Pub. Utils. Comm'n* No. 08-674 (cert. stage) at 11-12 (Mar. 18, 2009).

Furthermore, under the application of the court of appeals' decision envisioned by the Nevada BCP in *Morgan-Stanley*, a non-contracting party may wait until a contracting party has filed a complaint—indeed, may wait until after a court of appeals has remanded a Commission decision on a contracting party's complaint—and only then step in to request FERC to invalidate a contract under the ordinary just-and-reasonable analysis. *See* Nevada BCP Answer at 11 (arguing that Commission could apply ordinary just-and-reasonable standard, even

though "the third-party issue was not addressed on appeal," because "[o]nce the Commission reacquires jurisdiction of a remanded decision, it has the discretion to reconsider the whole of its original decision"). But regardless whether a non-party is permitted to piggyback off an existing complaint in that manner, under the decision below, extended litigation and high litigation costs would be the norm—and freely entered contractual relations could not be counted upon to justify capital investments or other resource commitments necessary to produce power in needed amounts.

2. The turmoil occasioned by the decision below would be especially burdensome for power marketers. In that intensely competitive business, profit margins are modest and will be substantially eroded if the contracts that are most favorable to a seller can be enforced, if at all, only by spending large sums on litigation. As FERC has recognized, when power marketers undertake their operations—even in a system in which contracts are regularly enforced—they "assume significant risk." *Citizens Power & Light Corp.*, 48 F.E.R.C. ¶ 61,210, at 61,776 (Aug. 8, 1989). They may "purchase products for which [they have] no immediate buyer, or . . . commit to sell products before [they have] a guaranteed purchase." *Id.* And because they own no transmission or generation facilities, power marketers have "no rate base on which to earn a traditional rate of return" and subsidize any losses they incur in trading. *Id.* For power marketers in particular, therefore, success in the energy market depends entirely on their ability to capitalize on the contracts they make to buy and sell at certain rates. A regulatory

environment that creates uncertainty about contract enforcement, and thus impedes the ability to manage risk, will tend to raise the costs, reduce the financial rewards, and increase the risks of companies that trade in wholesale power markets.

The decision below severely impedes contracting parties' ability to manage the risk posed by the ordinary just-and-reasonable standard. As this Court's precedent makes clear, contracting parties have always been free to contract around the *Mobile-Sierra* "public interest" standard by negotiating for the inclusion of so-called "*Memphis* clauses" that permit a party to petition FERC at any time to adjust agreed-upon rates under the ordinary just-and-reasonable standard. *See Memphis Light, Gas & Water Div.*, 358 U.S. at 112; *see also Williston Basin Interstate Pipeline Co. v. FERC*, 519 F.3d 497, 499 (D.C. Cir. 2008) (discussing origin of *Memphis* clauses). Before the D.C. Circuit's opinion in this case, power marketers (like any market participant) could induce other contracting parties to forgo the protection of a *Memphis* clause and lock in agreed-upon rates by offering more attractive contract terms than they might otherwise make available under the ordinary just-and-reasonable standard. In other words, the parties to each and every contract could decide for themselves whether they wished to be bound—or not to be bound—by *Mobile-Sierra*.

Under the decision below, in contrast, every contract effectively has a built-in *Memphis* clause for non-parties, denying both sellers and buyers the ability to negotiate for the certainty *Mobile-Sierra* affords. And FERC has, "in light of the *Maine PUC* decision," required replacement of "provisions that

seek to impose a 'public interest' standard of review on non-contracting third parties," with "a substitute provision that imposes on non-contracting third parties 'the most stringent standard permissible under applicable law,'" *Duke Energy Carolinas, LLC*, 123 F.E.R.C. ¶ 61,201 at P 10 & n.10 (2008). *See* Pet'r Reply Br. (cert. stage) at 5 (citing examples in Reply App. 1a-10a).

Rather than increasing risk premiums to reflect the uncertainty caused by voidable contracts, moreover, power marketers may simply refrain from offering forward supply contracts and commit their capital to other markets that entail less risk. Like power producers or distribution companies, which will likely refuse to invest the significant amounts of capital required to create or replace capacity in an uncertain market, firms that function principally as power marketers have broad flexibility on the extent to which they will continue to engage in that business, because they buy and sell wholesale power that will ultimately be produced or distributed by others.

If that were allowed to happen, the cost to the electric power industry, and to the public, which depends on that industry daily, will be very large. As "deal-maker[s] and risk-taker[s]," power marketers must "focus on efficiency enhancing trades because [they] cannot survive unless [they] do." *Citizens*, 48 F.E.R.C. at 61,777. As such, power marketers "can increase efficiency in power supply markets and in turn ultimately lower the cost of electricity." *Id.*

3. What is more, the uncertainty engendered by the court of appeals' approach would make power marketers and other sellers least likely to enter into

long-term energy contracts precisely when the need for such contracts (and energy generally) is at its greatest. During times of high energy price volatility, like the Western energy crisis that spurred the litigation in *Morgan Stanley*, sensible regulatory policies encourage long-term contracts, which allow "buyers and sellers [to] lock in prices over an extended period," and thus "hedg[e] and allocat[e] risk to specialists willing and able to take on that risk." *Nev. Power Co. & Sierra Pac. Power Co. v. Enron Power Mktg., Inc.*, 101 F.E.R.C. ¶ 63,031, at 65,287 (Dec. 19, 2002); *see Morgan Stanley*, 128 S. Ct. at 2743 (noting that part of FERC's "emergency effort" to combat the crisis in the West was "to shift . . . purchases to the forward market" and to encourage investor-owned utilities "to enter into long-term contracts").

In a system where every contract is subject to a post-hoc challenge for "reasonableness" by a non-party, however, buyers will be hard-pressed to find any seller willing to take such a risk. That is because, when market prices are notably high, the likelihood that prices will decline in the future is correspondingly great, and the risk of suit from customers who become unhappy with their utilities' long-term deals would impose costs too high to make such sales worthwhile. The decision below, therefore, will discourage deals at the time when the public is most in need of a stable supply of energy. Combined with the decreased participation of power marketers generally, and the inability to attract capital for development moving forward, the consequences of the turmoil induced by the court of appeals' bifurcated approach to contractual reasonableness will severely

undermine the efficacy of the power markets and harm the consumers that must rely on them.

4. Because the court of appeals misinterpreted the *Mobile-Sierra* standard to apply only to rate challenges brought by contracting parties, it had no occasion to address respondents' alternative argument that the rates agreed to in the forward capacity market auctions and the transition payments in the settlement agreement fail to constitute contract rates entitled to *Mobile-Sierra* protection. *See* Opp. at 10-12. This Court need not and should not reach that question. *See F. Hoffmann-La Roche Ltd. v. Empagran S.A.*, 542 U.S. 155, 175 (2004) ("The Court of Appeals . . . did not address this argument, . . . and, for that reason, neither shall we.") (internal citation omitted). As petitioners have explained, *no* court has addressed whether these types of auctions and payments constitute contracts to which *Mobile-Sierra* attaches. Pet'r Br. 46. It would thus be especially prudent in this case to allow the court of appeals to address that issue (if at all) in the first instance. *See Cutter v. Wilkinson*, 544 U.S. 709, 718 n.7 (2005).

In any event, the arguments advanced by the government in this Court provide no reason to question the applicability of *Mobile-Sierra* to the forward capacity auction results provided for in the parties' settlement. While acknowledging that the capacity auction results "possess[] certain characteristics of contracts," the government nonetheless contends that they "do not constitute contracts" because they "are not recorded in separate agreements between a particular generator and a particular purchasing entity" and "do not specify the consequences of default."

Gov't Br. 30. But this Court has never suggested that application of *Mobile-Sierra* could turn on the way in which multiple parties choose to record their agreed-upon rates or how parties specifically plan for any breach of their agreements. Nor is there any principle in contract law that makes those considerations salient. *See* Joseph M. Perrillo, *Corbin on Contracts*, § 52.1, at 278 (2005) ("Two or more may contract with one, together making a promise to her . . . . [they] may as a group all promise that a single performance shall be rendered, or they may each promise a separate performance."); *id.* § 58.1, at 397 (explaining that only "under certain conditions" can parties "determine in advance what damages will be assessed in the event of a breach").

The *Mobile-Sierra* standard, as the government recognizes, rests upon the "presumption that rates set out in a freely-negotiated whole-sale energy contract are just and reasonable." Gov't Br. 14. In a related case, the court of appeals has suggested that the auctions at issue in this case will result in just and reasonable rates, just as would other contractual negotiations. *See Conn. Dep't of Pub. Util. Control v. FERC*, Nos. 07-1375, 07-1460, 08-1175, 2009 WL 1754607, at *4 (D.C. Cir. June 23, 2009) ("[T]he purpose of the Forward Market is only to locate the price at which market incentives will be sufficient to meet th[e] expected demand [for capacity]."). If the Court elects to reach this question of first impression, therefore, the formalities emphasized by the government afford no basis for denying the market the stability *Mobile-Sierra* demands for a fairly negotiated rate. Rates agreed upon by "'sophisticated businesses enjoying presumptively equal bargaining

power,'" *Morgan Stanley*, 128 S. Ct. at 2746 (quoting *Verizon Commc'ns Inc. v. FCC*, 535 U.S. 467, 479 (2002)), are presumptively just and reasonable and reviewed under the public interest standard, regardless of the particular form in which they may be memorialized.

CONCLUSION

For the foregoing reasons, as well as those stated by petitioners, the Court should reverse the decision of the court of appeals.

Respectfully submitted,

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AMICUS CURIAE BRIEF

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NRG POWER MARKETING, LLC, ET AL.,

Petitioners,

v.

MAINE PUBLIC UTILITIES COMMISSION, ET AL.,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF AMICI CURIAE PUBLIC CITIZEN, INC., AND AARP IN SUPPORT OF RESPONDENTS

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INTEREST OF AMICI CURIAE

Public Citizen, Inc., is a consumer advocacy organization founded in 1971.[1] On behalf of its members nationwide, Public Citizen appears before Congress, administrative agencies, and the courts on a wide range of issues and works toward enactment and effective enforcement of laws and regulations protecting consumers, workers, and the general public. As relevant to this case, Public Citizen is particularly concerned with protecting the interests of retail electricity customers, who ultimately bear the costs of wholesale electricity rates that are, at least nominally, regulated by the Federal Energy Regulatory Commission (FERC). Because unjust and unreasonable wholesale electricity rates are almost invariably passed on to retail customers, proper enforcement by FERC of the provisions of the Federal Power Act (FPA) that outlaw unjust and unreasonable rates is critical to the protection of the consumers whom the FPA was primarily intended to benefit. Public Citizen has therefore participated, and continues to participate, in litigation challenging FERC's so-called "market-based rate" system, which deviates from the requirements of the FPA in many critical respects.

AARP is a nonpartisan, nonprofit organization that helps people over the age of 50 to have independence, choice, and control in ways that are beneficial to them and society as a whole. AARP has

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[1] Letters of consent to the filing of this brief from all parties are on file with the Clerk. The brief was not authored in whole or in part by counsel for a party, and no person or entity other than the amici curiae or their counsel made a monetary contribution to its preparation or submission.

nearly 40 million members. AARP is greatly concerned about the threats to health and safety of America's most vulnerable citizens caused by the recent sharp rise in energy costs. Because the cost of utilities has skyrocketed, many low and middle-income families and older people must now choose between paying their energy bills for heating and cooling and paying for other essentials such as food and medicine. AARP therefore works in both Congress and the states to protect consumers from excessive rates and charges. As consumers, AARP members depend upon the protection from excessive rates that the FPA affords when it is effectively administered by FERC—protection founded on the FPA's core command that rates be just and reasonable.

Both Public Citizen and AARP previously submittted or joined in the submission of briefs to this Court as amici curiae in *Morgan Stanley Capital Group v. Public Utility District No. 1*, 128 S. Ct. 2733 (2008), which like this case concerned the scope of the Court's 1956 decisions in *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332 (*Mobile*) and *FPC v. Sierra Pacific Power Co.*, 350 U.S. 348 (*Sierra*). The amici curiae now submit this brief because the positions taken by FERC and the petitioners in this case are, if anything, even more damaging to the protection of the public than FERC's embrace of "market-based rates." The expansion of the *Mobile-Sierra* doctrine that FERC and petitioners advocate would effectively nullify the consumer protection goals of the FPA by imposing a virtually insurmountable obstacle to challenging wholesale

electricity contracts that result in unjust and unreasonable rates paid by consumers.

SUMMARY OF ARGUMENT

The FPA regulates wholesale electricity rates with the objective of protecting the ultimate consumers of electricity by guaranteeing that rates are "just and reasonable." Far from substituting a regime of sanctity of contract for that statutory bond of protection, the "*Mobile-Sierra* doctrine" has, through most of its history, provided only that power sellers dissatisfied with rates they agreed to in contracts could escape their improvident bargains only if they demonstrated that the rates were unlawful under the FPA, and could meet that burden only by invoking the interests of the public, not their own private interests. Even as more recently extended in *Morgan Stanley* (and a handful of lower court decisions preceding it) to impose a similar burden on wholesale buyers, the doctrine has never been deemed to create a "presumption" that rates are just and reasonable when challenged by consumers, public authorities, or others who were not parties to the contracts establishing them. Petitioners and FERC are therefore wrong to suggest that there is a long history of protecting contractually established rates against challenges by third parties under the normal statutory "just and reasonable" standard.

Nor does the reasoning of this Court's decision in *Morgan Stanley* support the creation of a weighty "presumption" that consumers and other non-parties to wholesale power contracts must overcome in challenging contractually specified rates as unjust and unreasonable. According to *Morgan Stanley*, the *Mobile-Sierra* doctrine rests on the notion that parties

to such contracts can be expected to protect their own private interests, and thus that the lawfulness of rates set in wholesale electricity contracts should be assessed on the basis of their justness and reasonableness to the *public*. There is no basis for the further leap that contracting parties can also be expected to protect the interests of the public. Indeed, there is every reason to believe that they will not, because wholesale purchasers who resell power to consumers are typically entitled to pass on their costs directly to consumers, and thus have reduced incentives to minimize costs. Thus, where members of the public or their representatives are asserting their own rights under the FPA to have FERC determine the lawfulness of rates that directly affect their interests, neither *Mobile-Sierra* nor *Morgan Stanley* supports the imposition of any heightened burden on them. The unmodified statutory standard—whether rates are just and reasonable—governs such challenges.

ARGUMENT

I. This Case Is Not an Appropriate Vehicle for Making Sweeping Rulings About the Scope of the *Mobile-Sierra* Doctrine.

FERC argues convincingly in its brief that the *Mobile-Sierra* doctrine does not, of its own force, apply to the capacity rate-setting mechanisms established by the settlement agreement at issue in this case. *See* FERC Br. 24-32. Nonetheless, FERC joins the petitioners in inviting this Court to reverse the decision of the court of appeals based on broad propositions about the application of the *Mobile-Sierra* doctrine to third-party challenges to rates established in wholesale electricity contracts—even

though, as FERC acknowledges, that is not, properly speaking, what this case is even about.

FERC has it precisely backwards. If, as FERC maintains, the rate-setting arrangements in this case are not ones to which the FPA requires application of the *Mobile-Sierra* doctrine at all, this case cannot be the appropriate arena for determining whether the FPA somehow requires extending the application of the *Mobile-Sierra* doctrine to third-party challenges to wholesale rate contracts or, if it does, what the doctrine means in the context of such a challenge.

Instead, the issue should be whether the Commission may, in approving a settlement agreement, prospectively limit the rights of third-parties who may challenge future capacity rates established using the mechanism created by the settlement, by calling for the application of a "public interest" standard derived from the *Sierra* decision to complaints that those rates are unjust and unreasonable under section 206 of the FPA (16 U.S.C. § 824e).[2]

To that more limited question (if it falls within the scope of the question presented), the answer is no. Nothing in the FPA authorizes FERC to accept a settlement (and a contested settlement at that) that does not satisfy the just and reasonable standard. And "that [a] proposal is a settlement does not 'estab-

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[2] The two key provisions of the FPA involved here are section 205, codified at 16 U.S.C. § 824d, and section 206, codified at 16 U.S.C. § 824e. For ease of reference, we henceforth use the U.S. Code rather than FPA section numbers in this brief, as the Court did in *Morgan Stanley* and FERC does in its brief in this case.

lish without more the justness and reasonableness of its terms.'" *Tejas Power Corp. v. FERC*, 908 F.2d 998, 1003 (D.C. Cir. 1990) (quoting *Mobil Oil Corp. v. FPC*, 417 U.S. 283, 312-13 (1974)). Nor is there any reason for establishing a "presumption" that capacity rates established through the settlement mechanisms will in any way reflect some representation of the interests of consumers (or state agencies or other third parties) that could justify any expectation that the resulting rates will be "just and reasonable" as to them. *Cf. Morgan Stanley*, 128 S. Ct. at 2746 (quoting *Verizon Commc'ns Inc. v. FCC*, 535 U.S. 467, 479 (2002)). In its order approving the settlement, FERC identified no such reason for applying the statutory just and reasonable standard less stringently to complaints by third parties.

II. The *Mobile-Sierra* Doctrine Creates No "Presumption" That Rates Are Just and Reasonable from the Standpoint of Non-Parties to a Contract.

Assuming for the sake of argument that issues as to the scope of the *Mobile-Sierra* doctrine, where it applies of its own force to a contractually established rate, are properly before the Court, the argument of FERC and the petitioners that the doctrine limits the ability of non-parties to a contract to complain that rates are unjust and unreasonable *as to them* or that it creates a heightened "presumption" of legality of contract rates that binds non-parties, is wholly unwarranted. It finds support neither in the FPA itself nor in the *Mobile-Sierra* doctrine's construction of the FPA—even the expansive version of that doctrine adopted by the Court in *Morgan Stanley*.

A. Petitioners' Assertion That the *Mobile-Sierra* Doctrine Has Long Limited Claims That Contractually Established Rates Are Unjust and Unreasonable to Consumers Is Historically Inaccurate.

Central to petitioners' and FERC's argument is the notion that the FPA has long been interpreted to erect a heightened barrier to consumers and other non-parties who seek to have contractually based wholesale electric rates modified on the ground that they are unjust and unreasonable. Based on this supposedly settled understanding of the FPA, petitioners assert that the power industry will face massive disruption unless non-parties challenging rates are held to as stringent a standard as sellers seeking to free themselves from an "improvident bargain." Pet. Br. 6 (quoting *Sierra*, 350 U.S. at 355).

Petitioners' and FERC's position is historically inaccurate. Until this Court's decision only last year in *Morgan Stanley*, the application of *Mobile-Sierra* to purchasers under wholesale electricity contracts was itself supported only by a scant handful of recent judicial decisions. There is even less basis for extending the doctrine still further to erect a "presumption" applicable to non-parties challenging rates they neither bargained for nor agreed to. Indeed, even the recent decisions predating *Morgan Stanley* that had applied *Mobile-Sierra* to claims made by buyers under wholesale electricity contracts acknowledged that FERC must remain solicitous of the interests of consumers who are the ultimate intended beneficiaries of the FPA. There is no warrant for abandoning that solicitude and imposing on consumers a heightened burden when they seek to protect their rights under

the FPA to insist that rates ultimately passed on to them be just and reasonable.

1. The Federal Power Act and the Origins of *Mobile-Sierra*

The legal framework against which *Mobile* and *Sierra* were decided is the FPA. The Act regulates "the sale of electric energy at wholesale" (i.e., "sale of electric energy to any person for resale"). 16 U.S.C. §§ 824(b)(1), (d). The bedrock command of the FPA is set forth in 16 U.S.C. § 824d(a):

> All rates and charges made, demanded, or received by any public utility for or in connection with the transmission or sale of electric energy subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

"Public utility," as used in § 824d(a), is a term of art under the FPA, referring to entities that own or operate facilities for wholesale *sale* (or transmission) of electricity in interstate commerce. 16 U.S.C. §§ 824(b)(1), (e).[3] Thus, in the FPA, "public utility" does not simply refer generically to electric power companies, nor does it describe what many people may normally think of as "utilities"—that is, compa-

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[3] Such facilities, in the case of wholesale power marketers, who own neither generation units nor power lines but buy and sell power at wholesale, may simply be the contracts that they use to acquire and resell power. *See Automated Power Exch., Inc. v. FERC*, 204 F.3d 1144, 1151-52 (D.C. Cir. 2000).

nies that sell electricity at retail to the consumers who actually use it and that are typically regulated (or, today, deregulated) by the states.

Although the FPA directly regulates wholesale rates and transactions and the sellers who engage in them, its reason for doing so is that such sales are "for ultimate distribution to the public" and thus are "affected with a public interest." *Id.* § 824(a). As this Court has repeatedly recognized, "[a] major purpose of the whole Act is to protect consumers against excessive prices." *Pa. Water & Power Co. v. FPC*, 343 U.S. 414, 418 (1952). The FPA's provisions, like the parallel provisions of the Natural Gas Act, are aimed at "afford[ing] consumers a complete, permanent and effective bond of protection from excessive rates and charges." *Atl. Refining Co. v. Public Serv. Comm'n*, 360 U.S. 378, 388 (1959). Thus, consumers are supposed to be FERC's "prime constituency" in its administration of the FPA, *Md. People's Counsel v. FERC*, 761 F.2d 780, 781 (D.C. Cir. 1985), and each provision of the Act "must be read in light of the Federal Power Act's primary purpose of protecting the utility's customers." *Elec. Dist. No. 1 v. FERC*, 774 F.2d 490, 492-93 (D.C. Cir. 1985) (Scalia, J.).

The Act accomplishes its ends by requiring that public utilities (i.e., wholesale sellers of power) must file schedules setting forth their rates and charges, as well as all contracts establishing or affecting such rates and charges, with FERC. 16 U.S.C. § 824d(c). When a public utility changes a rate, charge or contract, it must provide advance notice, and FERC may investigate and set for hearing the question whether the change is lawful (that is, "just and reasonable" as required by § 824d(a) and not preferential in viola-

tion of § 824d(b)). *See* 16 U.S.C. §§ 824d(d), (e). FERC may also suspend the effect of the change for a limited time pending hearing and/or, if the new rate goes into effect and is then held unlawful, order refunds. *Id.* § 824d(e). Even after a rate or contract goes into effect, § 824e provides that FERC at all times retains authority, upon its own initiative or upon a complaint filed by anyone, to find that the rate or contract is "unjust, unreasonable, unduly discriminatory or preferential." If FERC so finds it must "determine the just and reasonable rate ... or contract to be thereafter observed and in force, and shall fix the same by order." 16 U.S.C. § 824e(a).

In *Mobile*, this Court considered whether, under the parallel provisions of the Natural Gas Act, a seller that had entered into a contract obligating it to provide gas at a particular rate could unilaterally supersede that contract just by filing with the Commission a schedule setting forth a new, higher rate subject to Commission review. The Court, not surprisingly, said no. The Act, the Court held, permitted rates for particular customers "to be established initially by contract," 350 U.S. at 339, subject, like "any other rate," to being "set aside" if "found unlawful by the Commission." *Id.* at 342. Nothing, however, in the Act's provisions authorizing (and, indeed, requiring) the filing of rates and contracts, empowered sellers "to change their contracts unilaterally" just by purporting to make a new rate filing in violation of the contract already on file. *Id.* at 340.

Sierra, decided the same day, took *Mobile* a step further. In *Sierra*, a wholesale electricity supplier sought to escape a contract in which it had committed to sell power to a buyer at a rate it now thought

unreasonably low. To that end it, like the seller in *Mobile*, attempted to avoid its contract by unilaterally filing a new rate schedule. *Sierra* began by holding that the FPA, like the Natural Gas Act, did not permit a public utility (i.e., a wholesale power seller) to change its contracts unilaterally by filing new rate schedules. 350 U.S. at 353. The *Sierra* Court, however, had to address an additional question: whether the Commission had effectively found the old contract rate unlawful and exercised its power under § 824e to replace it with a new, lawful rate (namely, the one filed by the seller). *See id.* The seller argued that the Commission had made such a finding by determining that the seller's rate of return on the contract was unreasonably low, while the rate of return under the rate schedule the seller was attempting to substitute for the contract was reasonable.

The Court rejected the seller's argument, holding instead that:

> [W]hile it may be that the Commission may not normally impose upon a public utility a rate which would produce less than a fair return, it does not follow that the public utility may not itself agree by contract to a rate affording less than a fair return or that, if it does so, it is entitled to be relieved of its improvident bargain. ... In such circumstances the sole concern of the Commission would seem to be whether the rate is so low as to adversely affect the public interest—as where it might impair the financial ability of the public utility to continue its service, cast upon other consumers an excessive burden, or be unduly discriminatory. That the purpose of the power given the Commission by § [824e(a)]

> is the protection of the public interest, as distinguished from the private interests of the utilities, is evidenced by the recital in § [824] of the Act that the scheme of regulation imposed "is necessary in the public interest." When § [824e(a)] is read in the light of this purpose, it is clear that a contract may not be said to be either "unjust" or "unreasonable" simply because it is unprofitable to the public utility.

350 U.S. at 355.

The holding of *Mobile* was by its nature limited to sellers, because purchasers of power obviously cannot unilaterally file rate schedules regardless of whether they are parties to a contract. *Sierra*, too, stated its holding in terms applicable to sellers of power: It said that a "public utility"—that is, a seller for resale, a wholesaler—could not seek to have the Commission overturn a rate it had agreed to by contract unless the rate was "so low as to adversely affect the public interest." *Id.* at 355. Moreover, given the FPA's objective of protecting consumers, it was not surprising that the Court concluded that the circumstances in which the Act's goals would be impaired by *low* rates would be quite unusual, and that lack of profitability for the seller was not sufficient to render a rate it had "improvidently" agreed to unlawful. *Id.*

2. *Mobile-Sierra* in the Courts

In the decades immediately following the announcement of what has come to be known as the *Mobile-Sierra* doctrine, there is no sign that courts or the Commission viewed it as erecting any heightened standard for challenges to rates by purchasers of

power, let alone by consumers adversely affected by high rates. In one of the first appellate decisions issued after *Mobile* and *Sierra*, the Fourth Circuit held that those decisions did not apply to a claim that a contract rate was unlawful under the FPA because it was too high, and this Court denied certiorari. *S.C. Generating Co. v. FPC*, 249 F.2d 755 (4th Cir. 1957), *cert. denied*, 356 U.S. 912 (1957).

This Court's subsequent decisions applying and elaborating the doctrine, like *Mobile* and *Sierra* themselves, concerned the circumstances in which sellers could be relieved of contract rates they claimed were too low. Those decisions established that sellers could, by contract, preserve their right to file rate changes (subject to Commission review under the ordinary just and reasonable standard), *see United Gas Pipe Line Co. v. Memphis Light, Gas & Water Div.*, 358 U.S. 103 (1959), and that absent such provisions in the contract, a seller could obtain a Commission order invalidating its contract rates as too low only in what the Court described as cases of "unequivocal public necessity." *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 822 (1968).[4]

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[4] *Permian Basin*, like *Memphis*, *Sierra*, and *Mobile*, was a case where sellers sought to be relieved of rates they considered too low, and the Court there emphasized that it was important to the scheme of regulation to hold "regulated companies"—i.e., sellers—to their contracts. 390 U.S. at 822. We recognize that in *Morgan Stanley*, the Court held that the same principle extended to buyers. Our point is not that *Morgan Stanley* was incorrect in so holding (though obviously we advocated a different result in that case), but that for most of the history of the *Mobile-Sierra* doctrine, it was not so applied.

The lower courts, too, regularly described the doctrine as it was set forth in *Mobile* and *Sierra* themselves, as a limit on the ability of a public utility to file a rate schedule that raised rates in derogation of a contract binding the seller to a stated lower rate. For example, the D.C. Circuit summed up its understanding of the doctrine in a widely quoted passage in *Richmond Power & Light v. FPC*, 481 F.2d 490, 493 (D.C. Cir. 1973):

> The rule of *Sierra*, *Mobile* and *Memphis* is refreshingly simple: The contract between the parties governs the legality of the filing. Rate filings consistent with contractual obligations are valid; rate filings inconsistent with contractual obligations are invalid.

The same court similarly stated that *Mobile* and *Sierra*, "read conjunctively, make it crystal clear that the Commission possess only limited power to *raise prices* ... above those contractually fixed by the parties." *Pub. Serv. Comm'n v. FPC*, 543 F.2d 757, 790 (D.C. Cir. 1975) (emphasis added).[5] Or, as Judge Leventhal put it, the *Mobile-Sierra* doctrine provided that the FPA's provisions "do not authorize the Commission to approve unilateral rate increases that are inconsistent with a seller's contractual obligations." *Gulf States Utils. Co. v. FPC*, 518 F.2d 450, 452 (D.C. Cir. 1975).[6] *Accord, e.g., Papago Tribal*

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[5] The court cited this Court's decision in the *Permian Basin Area Rate Cases* as an example of the application of *Mobile-Sierra* to prevent sellers from raising rates above those set forth in contracts. *Id.* at 792.

[6] As *Gulf States* illustrates, the bulk of litigation in the lower courts, particularly after this Court's decision in *Memphis*,

(*Footnote continued*)

Util. Auth. v. FERC, 610 F.2d 914, 929-30 (D.C. Cir. 1979). Although the D.C. Circuit was the primary expositor of the *Mobile-Sierra* doctrine, other circuits also shared this understanding of its application.[7] The Commission, too, recognized that the *Mobile-Sierra* doctrine applied when a seller sought to escape rates it considered too low, and the standard imposed by *Sierra* was "whether the challenged rates 'are so low as to adversely affect the public interest.'" *Phil. Elec. Co.*, 58 F.P.C. 88, 90 1977 WL 17458 (1977) (quoting *Sierra*, 350 U.S. at 355). As the Commission put it, "Most of the judicial precedent dealing with the *Sierra* doctrine has addressed the question of the lawfulness of unilateral attempts to increase fixed rates in contravention of an effective contract." *Id.*

Moreover, decisions in the lower courts that, like *Permian Basin*, emphasized the heavy burden that a public utility must bear to satisfy the *Sierra* standard also arose in the context of efforts by sellers to raise rates. For example, *Papago Tribal Utility Au-*

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involved construction of contracts to determine whether they set forth fixed rates or whether they permitted sellers to file new rates unilaterally (but always "subject to [the Commission's] review powers under §§ [824d(e)] and [824e(a)]," 518 F.2d at 452). Thus, *Mobile-Sierra* really represents two different doctrines, the first concerning whether a seller has waived by contract its ability to make unilateral rate filings, and the second concerning the standard for review of contractually established rates under § 824e when challenged by a party to the contract who has waived the right to file unilaterally.

[7] *See, e.g., City of Fulton v. United States*, 680 F.2d 115, 120 (Ct. Cl. 1982); *Pennzoil Co. v. FERC*, 645 F.2d 360, 373-74 (5th Cir. 1981); *Pub. Serv. Co. v. FPC*, 557 F.2d 227, 229 (10th Cir. 1977).

thority v. FERC, 723 F.2d 950 (D.C. Cir. 1983) (*Papago II*), where the court described the *Sierra* standard as "practically insurmountable" (*id.* at 954), was a case in which a wholesale electricity seller had sought FERC authorization to raise rates, and the issue was whether its contract permitted rate increases only under the "public interest" standard, or whether it allowed them when the Commission found that the existing rate was not "just and reasonable" to the seller under the unmodified statutory standard. The same was true in *Kansas Cities v. FERC*, 723 F.2d 82 (D.C. Cir. 1983), where the court called the standard "almost insurmountable." *Id.* at 87-88.[8]

As the D.C. Circuit elsewhere said, *Mobile* and *Sierra* "merely specify that heavy burdens must be met before contractually fixed low rates may be increased without the consent of the customer." *Town of Norwood v FERC*, 587 F.2d 1306, 1312 (D.C. Cir. 1978). It is, of course, hardly surprising that under a statute dedicated to the protection of consumers, claims that rates to which a seller has agreed are too low would rarely if ever prevail. The major authorities construing *Mobile-Sierra* do not suggest that a similar burden should be imposed where the claim is that rates are unjustly or unreasonably high from the standpoint of the consumers the FPA protects.

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[8] *See also E. Ky. Power Co-op v. FERC*, 489 F.3d 1299, 1309 (D.C. Cir. 2007) (describing *Mobile-Sierra* as a doctrine under which "utility providers" may "contractually relinquish" some of their "rate-filing freedom" and may increase rates above those specified by contract only when they satisfy the "practically insurmountable" public interest standard).

Indeed, the Commission rejected the existence of any such burden in its 1976 decision in *Electric & Water Plant Board v. Kentucky Utilities Co.*, 55 F.P.C. 2035, 0076 WL 159953. There, the Commission addressed an effort of a wholesale purchaser to have provisions changed in a fixed-rate contract it had agreed to (based on the argument that a fuel-adjustment clause in the contract was in conflict with an intervening Commission regulation). The Commission held that *Mobile* and *Sierra* were applicable to the purchaser only to the extent that it, like the seller, could not "unilaterally" abrogate a contract rate (a proposition obvious even without *Mobile* and *Sierra* because buyers cannot unilaterally file rates), and could be relieved of the contractual rate only if it were held unlawful under § 824e. *Id.* at 2042-43. But the Commission did *not* require the buyer in such circumstances to make any heightened showing in order to demonstrate the unlawfulness of rates under § 824e. Rather, the Commission stated that the standard applicable to challenges to contractually fixed rates was whether "'the rate [provided by the contract] is so low as to adversely affect the public interest—as where it might impair the financial ability of the public utility to continue its service, cast upon other consumers an excessive burden, or be unduly discriminatory' *or is so high that it exceeds a just and reasonable rate.*" *Id.* at 2042 (emphasis added; footnote omitted) (quoting *Sierra*, 350 U.S. at 355). That is, the unmodified statutory standard applied to a claim that the contract rate was unlawful because it was excessive.

Moreover, even the few and relatively recent lower court decisions, dating from the mid-90s, that

first applied *Mobile-Sierra* to claims by purchasers in wholesale energy transactions do not suggest that third parties—that is, consumers and the government agencies assigned the task of protecting them—who assert that a rate is unjust and unreasonable to them are held to a more stringent standard in demonstrating the unlawfulness of the rate than they would be in the absence of the contract.

For example, in *Northeast Utilities Service Co. v. FERC*, 993 F.2d 937 (1st Cir. 1993), which appears to be the first judicial decision squarely applying *Mobile-Sierra* to a purchaser's request that contractual rates be lowered,[9] the court held that FERC had wrongly applied the normal version of the just and reasonable standard rather than *Sierra*'s "public interest" variant in lowering the selling utility's rate of return, and it remanded to FERC for further explanation of its action. *Id.* at 961. In so doing, however, the court expressly noted that "the most attractive case for affording additional protection, despite the presence of a contract, is where the protection is intended to safeguard the interests of third parties, notably the buyer's customers." *Id.*

On remand, FERC adhered to its decision to reduce the contract rates. The agency repeated state-

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[9] In *Morgan Stanley*, the Court cited *Boston Edison Co. v. FERC*, 856 F.2d 361, 372 (1st Cir. 1988), as an instance of application of *Mobile-Sierra* to a purchaser's claim, but although the court in *Boston Edison* discussed *Mobile* and *Sierra*, the decision addressed a different, and narrower, question, namely the enforceability of a contractual clause providing that a purchaser had a limited amount of time to claim refunds of overcharges.

ments made in its earlier decision that it was "not aware of any court definitively holding that parties to a contract can waive the section [824e] rights of nonparties, and we believe that in cases where a nonparty challenges a rate contract in a section [824e] proceeding, it need only show that the contract is unjust, unreasonable, unduly discriminatory or preferential." *Ne. Utils. Serv. Co.*, 66 FERC ¶ 61332, at 62078, 1994 WL 92839 (1994). FERC further explained at length that prior cases (including most notably *Papago II*) that described the *Mobile-Sierra* standard as nearly "insurmountable," arose in the different context of claims that contract rates were unreasonably low, and that the Commission's paramount mission of protecting consumers required it to apply a more flexible standard when the claim was that rates were unreasonably high to the detriment of consumers. *See id.* at 62081-88.

Upon further review, the First Circuit sustained the Commission's order. *Ne. Utils. Serv. Co. v. FERC*, 55 F.3d 686 (1st Cir. 1995). In upholding FERC's application of a flexible, consumer-protective standard where an unreasonably high rate affected the interests of third parties (that is, consumer ratepayers), the court stated:

> The holding of *Sierra* is clear; what justifies protective action in the public interest by the Commission *when it is considering whether a contract rate is too low* is where the rate might impair the financial ability of the utility to continue to supply electricity, force electricity consumers to bear an excessive burden, or be unduly discriminatory. This definition of what is necessary in the public interest was formulated

> in the context of a *low-rate* case. It was not and could not be an across-the-board definition of what constitutes the public interest in other types of cases.

Id. at 690 (emphasis in original). Moreover, the court specifically rejected the argument that *Papago II*'s "practically insurmountable" dictum applied in cases where the public was adversely affected by too-high rates. *Id.* at 692.[10]

The D.C. Circuit, like the First Circuit, had held *Mobile-Sierra* applicable to claims by purchasers in a few recent cases preceding *Morgan Stanley*, but that court, too, had stopped far short of imposing a heightened burden on consumers or other non-parties in challenging a contract rate as unjustly or unreasonably high. For example, in *Texaco Inc. v. FERC*, 148 F.3d 1091 (D.C. Cir. 1998), the first case in which the D.C. Circuit held *Mobile-Sierra* applicable to a buyer's claim that a contract provision was unreasonable, the court held that FERC could not consider the contracting parties' own interests in determining the lawfulness of the contract, but it nonetheless *upheld* FERC's determination that the contract was unlawful under § 824e because it would "distort" pricing in the gas market and have anti-competitive effects on a third-party competitor of the buyer. *Id.* at 1097. The court nowhere suggested that had consumers, or the buyer's third-party competitor, com-

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[10] After the First Circuit's holding in *Northeast Utilities II*, FERC reaffirmed its view that contracts did not limit its authority to protect the interests of non-parties. *See S. Co. Servs., Inc.*, 67 FERC ¶ 61,080 (1994); *Fla. Power & Light Co.*, 67 FERC ¶ 61,141 (1994).

plained directly, they would have borne some elevated burden to demonstrate that the contract was unjust and unreasonable from the standpoint of their interests.

Similarly, in *Potomac Electric Power Co. v. FERC*, 210 F.3d 403 (D.C. Cir. 2000) (*Pepco*), which this Court cited in *Morgan Stanley* as an instance of the application of *Mobile-Sierra* to § 824e complaints brought by purchasers, see 128 S. Ct. at 2739, the D.C. Circuit quite pointedly refrained from suggesting that consumers who were not themselves parties to the contract containing the challenged rate would have had to show anything more than that it resulted in unjust and unreasonable rates if they had challenged it themselves. In *Pepco*, a retail power company brought a complaint under § 824e seeking to have rates under a contract for the purchase of transmission lowered to conform to rates that subsequently were offered by the seller under new "open access tariffs" instituted as a result of FERC's Order 888. The D.C. Circuit held that Pepco, the purchaser, was itself subject to the *Mobile-Sierra* standard and thus could not invoke its own interests to establish the unreasonableness of the contract. Acknowledging that courts and the Commission had taken a more protective approach where interests of consumers and other non-parties were at issue, the court rejected application of that approach to Pepco because "Pepco is not itself a non-party." *Id.* at 408-09. Moreover, the court noted, beyond simply asserting that it passed rates along to its retail customers, Pepco had neither shown, nor even attempted to show, that its ratepayers were adversely affected at all, or that they suffered undue discrimination or excessive bur-

den as a result of the challenged contract provisions. *Id.* at 409-10. Nowhere did the court suggest that, had rates paid by third parties actually been shown to be unjust and unreasonable under the conventional statutory standard, the contract would nonetheless have been upheld.

In sum, it is not the case, as petitioners and FERC contend, that the *Mobile-Sierra* doctrine reflects a consistent 50-year history of contract "sanctity" in the face of claims that rates resulting from wholesale power contracts are unjustly and unreasonable high. Rather, as originally articulated and applied by the courts for most of its history, the doctrine protected purchasers against attempts by sellers to raise rates unilaterally. And even as more recently extended to apply to claims by purchasers that rates are unlawfully high, the doctrine has foreclosed only claims that contracts were unreasonable from the standpoint of the interests of the purchasers themselves—that is, the actual contracting parties—not claims that contracts resulted in rates that were unjust and unreasonable to the consuming public whom the FPA was intended to protect.

B. *Morgan Stanley* Does Not Create a Presumption that Contract Rates Challenged by Non-Parties Are Lawful.

Morgan Stanley, of course, held that purchasers are subject to the *Mobile-Sierra* doctrine, but neither its holding nor its reasoning supports imposition of some new "presumption" that contract rates are just and reasonable to the members of the public who ultimately pay them but whose interests were not represented in the formation of the contracts themselves.

Rather, in holding that *Mobile-Sierra* applies to claims by purchasers that a contract rate is unjust and unreasonable, the Court in *Morgan Stanley* decided that what *Sierra* referred to as the "private interests" of the contracting companies themselves could not be considered in determining the lawfulness of their contracts. *Sierra*, 350 U.S. at 355. Nothing in that holding implies that where the public's interest in being free from unduly high rates is invoked, some heightened standard must apply.

Nor do the justifications for the *Mobile-Sierra* rule imply that consumers and other non-parties to contractual arrangements should face an increased "presumption" that rates they challenge are just and reasonable. *Mobile-Sierra* has been described as being based on a "broad waiver" of the contracting parties' right to have the Commission consider their interests in evaluating the fairness and reasonableness of the contract. *Papago II*, 723 F.2d at 953. But contracting parties cannot, by agreement, waive other people's rights, and thus cannot affect FERC's "indefeasible right," *id.*—indeed, its indefeasible statutory duty—to protect the public against unjust and unreasonable rates.

Morgan Stanley similarly reasoned that *Sierra* was "grounded in the commonsense notion that '[i]n wholesale markets, the party charging the rate and the party charged [are] often sophisticated businesses enjoying presumptively equal bargaining power, who could be expected to negotiate a "just and reasonable rate" *as between the two of them*.'" 128 S. Ct. at 2746 (quoting *Verizon*, 535 U.S. at 479) (emphasis added). Even assuming its debatable factual premise to be true, that justification only goes as far

as the interests of the parties themselves. Common sense may suggest that wholesale buyers and sellers "often" negotiate rates that are fair from the standpoint of their own particular interests (though the reverse may also "often" be true), but it hardly suggests that such rates will be fair from the standpoint of third parties.

Indeed, both common sense and long experience demonstrate that in transactions for the purchase and sale of wholesale electricity, companies that purchase power for resale to consumers can *not* be expected to negotiate rates that are just and reasonable to consumers, precisely because retail sellers of power have an almost unlimited ability to pass on rates to consumers. In particular, this Court's decisions in *Mississippi Power & Light Co. v. Mississippi*, 487 U.S. 354 (1988), and *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953, 970 (1986), nearly always guarantee that a wholesale rate that is filed with FERC (or satisfies the requirements that are said to pass for filing under FERC's new market-based rate regime) can be passed on to retail consumers notwithstanding any protections state law may attempt to provide consumers against unreasonable rates. Thus, wholesale purchasers have little incentive to minimize their costs. For this reason, "neither the Commission nor [the courts] may merely assume, without analysis, that the [wholesale purchasers'] protection of their own interests (if indeed they were able to protect them) will inure to the benefit of consumers; as regulated utilities, ... [they] might not have a sufficient incentive, in dealing with the [wholesale sellers], to minimize their costs." *Tejas*, 908 F.2d at 1003. In other words, the interests of

wholesale purchasers are not "sufficiently likely to be congruent with those of ultimate consumers" to justify treating their "agreement as dispositive of the consumers' interests." *Id.* at 1004.

Morgan Stanley's reasoning thus does not support imposing a "presumption" that contract rates challenged by consumers or other third parties are lawful. Even as extended in *Morgan Stanley*, the *Mobile-Sierra* doctrine is a "presumption" only in the limited sense that it imposes on parties to a contract a burden of showing something more than that the contract's rates are unjust and unreasonable as to them, based (according *to Morgan Stanley*) on an expectation that they would not agree to terms that are unfair *to themselves*. The "presumption," in other words, refers simply to the burden of demonstrating that the rates are unjust and unreasonable from the standpoint of the public as opposed to the private interests of the contracting parties.[11] Any such "presumption," however, is by its terms inapplicable when members of the public challenge contract rates as unjust and unreasonable to them. Put another way, *Mobile-Sierra*, as construed in *Morgan Stanley*, may require that the justness and reasonableness of

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[11] We note that other than one passing, off-hand reference to a "*Mobile-Sierra* presumption" in one D.C. Circuit opinion, *Union Electric Co. v. FERC*, 890 F.2d 1193, 1196 (D.C. Cir. 1989), the first time the doctrine was described by a court as establishing a "presumption" appears to have been in the pair of Ninth Circuit decisions that led to this Court's decision in *Morgan Stanley*, *Public Utilities District No. 1 v. FERC*, 471 F.3d 1053 (9th Cir. 2006), *vacated*, 128 S. Ct. 2993 (2008), and *Public Utilities Commission v. FERC*, 474 F.3d 587 (9th Cir. 2006), *aff'd*, 128 S. Ct. 2733 (2008).

contract terms be determined from the standpoint of the public, but it erects no "presumption" that such rates are consistent with the interests of the public.

Finally, in light of petitioners' and FERC's suggestion that extension of the *Mobile-Sierra* doctrine to encompass claims of non-parties is somehow necessary to support FERC's recent acceptance of so-called "market-based rates" under the FPA, a few observations on that subject are called for. To begin with, in this case, as in *Morgan Stanley* itself, the lawfulness of FERC's market-based rate regime is not before the Court. *See Morgan Stanley*, 128 S. Ct. at 2741, 2747. Indeed, the rates at issue are not market-based rates as FERC uses that term. As *Morgan Stanley* acknowledged, the lawfulness of FERC's market-based rate program is an open question, *see id.*, and in this case, as in *Morgan Stanley* itself, the Court should not purport to answer it when it is not properly presented by the case at bar.[12]

Moreover, far from being essential to carry out FERC's market-based rate program,[13] the interpre-

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[12] The principal legal infirmities in the market-based rate program were catalogued in the brief joined by amicus Public Citizen in *Morgan Stanley*, and we will not reiterate those points here. See Brief of Amici Curiae Colorado Office of Consumer Counsel, et al., No. 06-1457, at 15-20.

[13] Indeed, a doctrine that in its inception principally concerned the circumstances under which contracting parties were deemed to have waived the right to make unilateral rate filings seems singularly out of sync with a regulatory regime in which FERC has (albeit without statutory authority) largely dispensed with rate filings. *See Morgan Stanley*, 128 S. Ct. at 2741.

tation of *Mobile-Sierra* that petitioners offer here would render FERC's market-based rate regime superfluous, as it would allow even sellers ineligible to participate in that program (because they possess market power, for example) to immunize any rate they wish to charge from serious scrutiny whenever they have been able to find a buyer who will contract with them for power at that rate.[14] In short, the position of petitioners is, in effect, that the FPA is and always has been a program where the lawfulness of a rate was a question principally of what the market would bear. That has never been the law. Indeed, the FPA was enacted principally as a response to market failures that left consumers (and state regulators) "helpless against [utility] combinations," *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 610 (1944), not simply to ratify market outcomes. Holding that the interest in contract sanctity requires a "presumption" that rates in wholesale electricity contracts are just and reasonable from the standpoint of the public would turn the FPA's goal of "protect[ing] consumers against exploitation," *id.*, on its head.

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[14] Because the *Mobile-Sierra* doctrine applies to transmission as well as wholesale power contracts (*see, e.g., Pepco*), petitioners' position would effectively make unregulated freedom of contract predominant in transmission as well. Even FERC, however, concedes that transmission providers typically have market power that makes any semblance of a market-based rate regime for transmission unworkable. *See New York v. FERC*, 535 U.S. 1 (2002) (upholding FERC's Order 888, which imposes a variety of regulatory requirements on transmission as remedial measures under § 824e based in part on findings that transmission rates were unjust and unreasonable).

CONCLUSION

For the foregoing reasons, the decision of the court of appeals should be affirmed.

Respectfully submitted,

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AMICUS CURIAE BRIEF

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NRG POWER MARKETING, LLC, *ET AL.*,
Petitioners,

v.

MAINE PUBLIC UTILITIES COMMISSION, *ET AL.*,
Respondents.

On a Writ of Certiorari
to the United States Court of Appeals
for the District of Columbia Circuit

BRIEF OF THE PUBLIC UTILTIES COMMISSION OF THE STATE OF CALIFORNIA AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENTS

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QUESTION PRESENTED

Whether the Federal Energy Regulatory Commission is required, as a matter of law, to presume that all contract rates are just and reasonable, and therefore are lawful, absent "extraordinary circumstances," regardless of the identity of the challenger.

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INTEREST OF *AMICUS CURIAE*[1]

The California Public Utilities Commission (CPUC) is charged, under the Constitution of the State of California, with the regulation of public utilities, including retail electricity service providers, operating within the State of California. When necessary to protect consumers in California, the CPUC exercises its statutory right under the Federal Power Act, 16 U.S.C. § 791a *et seq.*, to participate in Commission proceedings and to challenge the lawfulness of wholesale energy contract rates, the cost of which affects the retail prices regulated by the CPUC. The question presented in this case may affect the standard of review applied in those federal proceedings and in any subsequent court challenge to the resulting wholesale rate.

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[1] Pursuant to Rule 37.6, counsel for *amicus* states that no counsel for a party authored this brief in whole or in part, and that no person other than *amicus*, its members, or its counsel made a monetary contribution to the preparation or submission of this brief. Petitioners and respondents have filed letters of consent with the Clerk of the Court.

SUMMARY OF ARGUMENT

Petitioners insist that the *Mobile-Sierra* doctrine[2] restricts the authority of the Federal Energy Regulatory Commission by requiring it to presume that a wholesale power contract is just and reasonable whenever that rate is challenged, whether the rate is contested by a party to the contract, a retail consumer, a state public utilities commission, or the Commission itself. They further insist that when *Mobile-Sierra* applies, the Commission must not only limit its review to considerations of the public interest, but must also presume, "absent extraordinary circumstances," that contract rates are consistent with the public interest and, therefore, lawful. *See* Petr. Br. 22-23 (citation omitted). Petitioners are in effect asking the Court to erect a "practically insurmountable" barrier, *Papago Tribal Util. Auth. v. FERC*, 723 F.2d 950, 954 (D.C. Cir. 1983) (Scalia, J.), that would prevent the Commission from modifying contract rates except in extraordinary circumstances. The Court should reject petitioners' request.

Petitioners misread this Court's cases. *Mobile* and *Sierra* are part of a line of decisions, culminating in *Morgan Stanley Capital Group Inc. v. Public Utilities District No. 1 of Snohomish County, Washington*, 128 S. Ct. 2733 (2008), that establish that buyer's or seller's remorse is no basis for the

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[2] *See United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332 (1956); *FPC v. Sierra Pac. Power Co.*, 350 U.S. 348 (1956).

Commission to alter the terms of a wholesale energy contract. That is, they stand for the simple proposition, recognized throughout this Court's cases, that the purpose of federal energy regulation is not to relieve a party of "its improvident bargain," *Sierra*, 350 U.S. at 355, or to "extricate [it] from a bed it made for itself," *Transcon. Gas Pipe Line Corp. v. State Oil & Gas Bd. of Miss.*, 474 U.S. 409, 425 (1986) (Rehnquist, J., dissenting). To be sure, in these cases the Court has also emphasized the importance of contract stability. But the Court has affirmed that this interest does not trump all others under the Act and that "*Mobile* recognized that there were two sources of price and supply stability inherent in the regulatory system . . . – the provisions of private contracts and the public regulatory power." *Sunray Mid-Continent Oil Co. v. FPC*, 364 U.S. 137, 155-56 (1960).

Petitioners' argument also is fundamentally at odds with the purposes and premises of the Federal Power Act. Wholesale electricity prices are largely set by contracts. As a result, accepting petitioners' argument that the Commission lacks the authority to modify contract rates except in extraordinary circumstances would result in substantial deregulation of the wholesale electricity market. But Congress did not enact the Federal Power Act simply to restrain the occasional aberrant contract. To the contrary, it subjected power sales to federal supervision because it believed that if left to their own devices, energy producers and utilities would negotiate rates inconsistent with the public interest. Petitioners' arguments for a contrary presumption are based on a fundamental disagreement with that

view. They insist that wholesale electricity markets can be expected to produce rates that are not only fair to the parties, but also consistent with the public interest. That Congress did not accept these assertions is plain and dispositive.

In fact, Congress's skepticism of energy markets' ability to produce prices consistent with the public interest is well-founded. Wholesale purchasers have limited incentives to bargain hard for low prices because under the filed rate doctrine, state regulators generally may not prevent them from passing the full cost of their wholesale contracts on to consumers. Moreover, because many utilities also have a state-imposed obligation to serve their retail consumers, they cannot simply walk away from a deal when confronted by excessive wholesale prices, conditions of market power, or limited available supply.

Petitioners nonetheless argue that without a guarantee that contract rates will almost never be modified, producers and utilities will not invest sufficiently in the nation's energy infrastructure. But the Act already gives substantial protection against unwarranted contract modification. As enacted, the statute permits and encourages challenges before rates go into effect and decisions are made in reliance on the contract. When challenges are brought later, the challenger bears the burden of demonstrating that the rate is unlawful. And, perhaps most importantly, Congress gave the Commission ample authority to reject such challenges when necessary to promote the public interest in contract stability and investor confidence.

Petitioners' request for the further protection of a strong presumption that all contract rates are just

and reasonable is inconsistent with Congress's decision to delegate principal rate review authority to an expert commission, rather than the courts. There is no reason to believe that Congress shared petitioners' distrust of the Commission's ability to determine how strongly adherence to contract prices is required to achieve the just and reasonable rates the statute commands.

The Commission's acquiescence to petitioners' proposed limitation of its authority is no reason to depart from the statutory scheme Congress enacted. While the Commission has expertise in setting utility rates, it has no special claim to deference for its interpretation of this Court's decisions in *Mobile*, *Sierra*, and *Morgan Stanley*. Moreover, its current view is of recent vintage and inconsistent with its prior position that the *Mobile-Sierra* presumption applies only to challenges by parties to the contract.

At the very least, no presumption should apply when the rate is challenged by a state public utility commission. State commissions have special expertise and legal responsibility for ensuring that utility rates are consistent with the public's competing interests in reasonable prices and the reliable supply that contract stability encourages. As a result, any general presumption that contract negotiations produce rates consistent with the public interest is more than overcome when an expert agency charged with protecting consumers determines that a particular rate has defied that expectation. The same should be true when the Commission itself initiates a rate review based on reasonable suspicions that the rate is unlawful.

ARGUMENT

Petitioners concede, as they must, that the Federal Energy Regulatory Commission has statutory authority to modify contracts when necessary to protect the public interest. Petr. Br. 4-5; *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332, 344 (1956). They contend, however, that the *Mobile-Sierra* doctrine requires the Commission to presume that rates in wholesale power contracts *are* in the public interest, and therefore just and reasonable, whenever a contract rate is challenged, regardless of the identity of the challenger. Petr. Br. 35. They contend further that under the *Mobile-Sierra* doctrine the Commission may find harm to the public interest sufficient to warrant contract modification "only in circumstances of *unequivocal public necessity*," which will occur only in "*extraordinary circumstances*." Petr. Br. 22-23 (citations omitted) (emphasis added).

These assertions are based on a fundamental misreading of this Court's cases, which simply hold that the Commission may not relieve disappointed buyers and sellers of their contractual obligations except in light of the broader public interest. Accepting petitioners' further assertion that the Commission is generally precluded from altering contract rates, even when they are challenged by third parties seeking to promote the public interest, would effectively deregulate much of the wholesale energy market, contrary to the basic purposes of the Federal Power Act.

I. This Court Has Never Held That The Commission Must Always Presume That Contract Rates Are Just and Reasonable.

Petitioners' claim that contract rates must be presumed just and reasonable and preserved absent extraordinary circumstances in all rate challenges has no support in this Court's cases.

A. The *Mobile-Sierra* Presumption Is Limited To Cases Of Buyer's Or Seller's Remorse.

1. In *Mobile* and *Sierra*, this Court recognized that by "requiring contracts to be filed with the Commission," the Federal Power Act "expressly recognizes that rates to particular customers may be set by individual contracts." *Mobile*, 350 U.S. at 338. At the same time, however, Congress obviously intended to permit the Commission to alter agreed-upon rates in appropriate circumstances, to protect the public. *See, e.g.*, 16 U.S.C. § 824e(a). The principal question in *Mobile* and *Sierra* was whether a seller may unilaterally abrogate a contract rate previously accepted by the Commission simply by filing a new rate schedule. *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332, 337-38 (1956); *FPC v. Sierra Pac. Power Co.*, 350 U.S. 348, 352-53 (1956). The Court held that it may not. The Act was not intended, the Court explained, to relieve parties of "improvident bargain[s]." *Sierra*, 350 U.S. at 355. Instead, the "purpose of the power given the Commission by [the Federal Power Act] is the protection of the public interest, as distinguished from the private interests of the utilities." *Id.*

Accordingly, *Mobile* and *Sierra* established nothing more than the principle that in reviewing challenges by parties to a contract, the Commission lacks the power to alter contract rates solely to protect the interests of a party. Instead, "[i]n such circumstances the sole concern of the Commission would seem to be whether the rate . . . adversely affect[s] the public interest." *Sierra*, 350 U.S. at 355. By limiting parties' abilities to use the statute to avoid their contract obligations, yet preserving the Commission's authority to modify rates in the public interest, this Court explained, the Act "affords a reasonable accommodation between the conflicting interests of contract stability on the one hand and public regulation on the other." *Mobile*, 350 U.S. at 344.

Nothing in these decisions suggests, much less holds, that maintaining the Act's intended balance requires equating a contracting party's attempt to evade its own improvident bargain with a third-party's request to modify a rate in order to protect the public interest. It is one thing to view with skepticism a contracting party's claim that the rate change it seeks is in the public interest. *See Mobile*, 350 U.S. at 344-45 (noting that contracting parties "are understandably not given the same explicit standing to complain of their own contracts as are those who represent the public interest or those who might be discriminated against"). Requiring especially convincing proof of harm to the public interest in challenges by contracting parties may well make sense in that context, for it does not unduly limit the Commission's "indefeasible right" to alter rates to protect the public interest, *Papago Tribal*

Util. Auth. v. FERC, 723 F.2d 950, 953 (D.C. Cir. 1983) (citing *Sierra*, 350 U.S. at 355), in response to challenges by non-parties to the contract or on its own initiative.

It is quite a different proposition, however, to say that the Commission must view all requests to modify contract rates with skepticism, regardless of who is seeking relief, and deny relief in all but extraordinary circumstances. As discussed below, imposing such a presumption in *every* contract rate challenge would be inconsistent not only with this Court's decisions in *Mobile* and *Sierra,* but with the basic purposes and design of the Federal Power Act.

2. Contrary to petitioners' suggestions, nothing in this Court's recent decision in *Morgan Stanley Capital Group Inc. v. Public Utilities District No. 1 of Snohomish County, Washington*, 128 S. Ct. 2733 (2008), is to the contrary.

As in *Mobile* and *Sierra*, the party challenging the contract rate was itself a party to the contract. This Court recounted that the respondents in the case had agreed to long-term contracts in the midst of unprecedented turmoil in the western energy markets. *Id.* at 2743. But "[a]fter the crisis had passed, buyer's remorse set in and respondents asked FERC to modify the contracts." *Id.* That factual context limited the Court's consideration to two questions relating to party-challenges to contract rate: "First, does the presumption apply only when FERC has had an initial opportunity to review a contract rate without the presumption? Second, does the presumption impose as high a bar to challenges by *purchasers* of wholesale electricity as it does to challenges by *sellers*?" *Id.* at 2737 (emphasis added).

The facts of the case did not pose, and this Court did not purport to decide, whether or how *Mobile-Sierra* would apply if the challenge were not brought by a party to the contract, much less whether the same analysis would apply to challenges brought by a state public utilities commission or the Commission itself. *See, e.g., id.* at 2747 (making clear that opinion was limited to addressing the proper application of the public interest test to "buyer's" and "seller's challenge[s]").

Moreover, as in *Mobile* and *Sierra*, the Court's rationale in *Morgan Stanley* turned principally on its recognition that Congress did not intend the Federal Power Act to alter contract rates just because they are "unfair to one of the parties that voluntarily assented to the contract." 128 S. Ct at 2746; *see also id.* at 2747 (criticizing court of appeals for "enabling sophisticated *parties* who weathered market turmoil by entering long-term contracts to *renounce those contracts* once the storm has passed") (emphasis added). In this way, the Court adhered to the principle, running throughout this Court's cases, that the federal energy regulatory regime was not created to "extricate [a utility] from a bed it made for itself." *Transcon. Gas Pipe Line Corp. v. State Oil & Gas Bd. of Miss.*, 474 U.S. 409, 425 (1986) (Rehnquist, J., dissenting).

To be sure, the Court also emphasized the importance of contract stability. But the decision did not suggest that this interest trumps all others under the Act or that it intended to depart from its prior acknowledgment that "*Mobile* recognized that there were two sources of price and supply stability inherent in the regulatory system . . . – the provisions

of private contracts and the public regulatory power." *Sunray Mid-Continent Oil Co. v. FPC*, 364 U.S. 137, 155-56 (1960). As discussed below, in asking the Court to declare that the Commission may not alter contract rates except in extraordinary circumstances, petitioners urge "an application of [the *Mobile* and *Sierra*] decision[s] that could make private contracts the only stabilizing factor under the Act." *Id.* at 155-56.

B. None Of This Court's Cases Preclude The Commission From Modifying Contract Rates Except In Extraordinary Circumstances.

Petitioners are also wrong in asserting that where it applies, the *Mobile-Sierra* doctrine prevents the Commission from altering contract rates at anyone's request absent "extraordinary circumstances." Petr. Br. 23 (citation omitted).

1. Although there may be grounds to presume that a contract rate negotiated by sophisticated utilities is just and reasonable "as between the two of them," *Morgan Stanley*, 128 S. Ct. at 2746 (citation omitted), there is no basis in this Court's decisions to require the Commission to presume that contract rates almost always serve the *public* interest and, therefore, are just and reasonable except in rare instances.

Certainly, the Court said nothing of the sort in *Mobile* or *Sierra*. To the contrary, the Court expressly recognized that denying companies "the power unilaterally to change their contracts in no way impairs the regulatory powers of the Commission, for the contracts remain fully subject to

the paramount power of the Commission to modify them *when necessary in the public interest.*" *Mobile*, 350 U.S. at 344 (emphasis added). And the Court said nothing about restricting the Commission's discretion in making that decision. Instead, it simply stated that "if the Commission, after hearing, determines the contract rate to be so low as to conflict with the public interest, it may . . . authorize the natural gas company to file a schedule increasing the rate." *Id.* at 345.

Likewise, in *Sierra*, the Court described the question before the Commission as whether "the rate is so low as to adversely affect the public interest – as where it might impair the financial ability of the public utility to continue its service, cast upon other consumers an excessive burden, or be unduly discriminatory." 350 U.S. at 355. Whether any of those conditions arose, or there were other grounds to find that the rate had an "adverse effect on the public interest," were questions the Court left to the Commission's discretion.

2. Petitioners nonetheless point to statements made in three subsequent cases that, they say, transformed the *Mobile-Sierra* doctrine into a nearly conclusive presumption that contract rates are just and reasonable (and therefore lawful), a presumption that precludes the Commission from modifying contract rates in almost all cases. Petitioners' reliance on that dicta is misplaced.

Petitioners first quote a single statement from *In re Permian Basin Area Rate Cases*, 390 U.S. 747 (1968), in which the Court described the Federal Power Act as "premised on contractual agreements voluntarily devised by the regulated companies" and

then stated in passing that the Act "contemplates abrogation of these agreements only in circumstances of *unequivocal public necessity*." *Id.* at 822 (emphasis added); *see* Petr. Br. 22. For this proposition, the Court cited *Mobile,* which, as shown above, imposed no such requirement. *See Permian Basin,* 390 U.S. at 822. Nor was the phrase "unequivocal necessity" necessary to the Court's decision in *Permian Basin* – the Court affirmed the Commission's refusal to set aside the contract rates in that case because there was "*no* evidence of financial or other difficulties" caused by the contract rate. *Id.* (emphasis added). And elsewhere in the opinion, the Court accurately described *Sierra* as holding only that the "Commission may not, absent evidence of *injury to the public interest*, relieve a regulated party of 'its improvident bargain.'" *Id.* at 821 (quoting *Sierra*, 350 U.S. at 355) (emphasis added). *See also id.* ("It follows that the Commission was here without authority to abrogate existing contract prices unless it first concluded that they '*adversely affect the public interest*.'") (emphasis added).

Next, petitioners cite *Arkansas Louisiana Gas Company v. Hall*, 453 U.S. 571 (1981), for the proposition that the Commission "lacks affirmative authority, absent *extraordinary circumstances*, to 'abrogate existing contractual arrangements.'" Petr. Br. 22-23 (quoting 453 U.S. at 582) (emphasis added). But again, the question of any presumption of lawfulness was not before the Court (the case did not involve a construction of *Mobile-Sierra*, but rather concerned an application of the filed rate doctrine, *see* 453 U.S. at 573). And the Court made the statement in the course of rejecting an interpretation of the

Natural Gas Act that – like petitioners' construction of the Federal Power Act – "would give inordinate importance to the role of contracts between buyers and sellers in the federal scheme for regulating the sale of natural gas" *Id.* at 582.

Finally, petitioners rely on *Morgan Stanley*, in which the Court repeated the dicta from *Permian Basin* and *Arkansas Louisiana Gas*, *see* 128 S. Ct. at 2748, and stated that "only when the mutually agreed-upon contract rate *seriously* harms the consuming public may the Commission declare it not to be just and reasonable," *id.* at 2746 (emphasis added); *see also id.* at 2747, 2750 (repeating the "seriously harms" formulation). The language of "serious harm" can be read simply to exclude insignificant effects on the public interest, which is a far cry from adopting a court-made rule restricting the Commission from modifying contracts except in "extraordinary circumstances," or upon a showing of "unequivocal necessity." That construction is consistent with *Mobile* and *Sierra*. In any event, the Court's mention in *Morgan Stanley* of "serious" harm was unnecessary to its rejection of the claim that a contract rate is inconsistent with the public interest whenever it is "above marginal cost." *Id.* at 2748-49.

II. To Require The Commission To Presume That Contract Rates Are Just And Reasonable, Except In Extraordinary Circumstances, Would Be Contrary To The Basic Premises Of The Federal Power Act.

Congress enacted the Federal Power Act to regulate what it saw as a heavily monopolistic market in which unregulated transactions routinely

risked serious harm to consumers and the broader economy. *See New York v. FERC*, 535 U.S. 1, 5-7 (2002); *see also FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 609-10 (1944). Petitioners' strained construction of this Court's decisions reflects a fundamental disagreement with that policy choice, and the rule they propose would go far toward dismantling the regulatory regime Congress intended.

A. Petitioners' Proposed Standard Would Effectively Deregulate Much Of The Wholesale Electricity Market.

1. Effective regulation cannot "turn on the desire of the regulated enterprise to be subject to it." *Sunray Mid-Continent Oil Co. v. FPC*, 364 U.S. 137, 151 (1960) (discussing regulation under Natural Gas Act). Yet accepting petitioners' arguments in this case would have that effect in many places. For example, in California, a market that serves over 33 million consumers, and other regions of the United States, the vast majority of wholesale electricity prices are set by bilateral contract. *See, e.g., Pub. Utils. Comm'n of Cal. v. FERC*, 462 F.3d 1027, 1039 (9th Cir. 2006) (noting that in "most . . . electricity markets . . . more than 80% of transactions are made through long term forward contracts"). Accordingly, requiring the Commission to presume that contract rates are just and reasonable, except in extraordinary circumstances, is to effectively deregulate markets Congress intended the Federal Power Act to regulate.

When Congress has directed an agency to regulate a market, the agency may not simply presume that the results the market produces meet

the applicable statutory standard, except in extraordinary circumstances. *See FPC v. Texaco, Inc.*, 417 U.S. 380, 394 (1974). No one would think, for example, that the courts have authority to require the Food and Drug Administration to presume, absent extraordinary circumstances, that drugs are safe and effective, 21 U.S.C. § 355(d), so long as they were produced in a competitive market. Congress adopted the Food, Drug, and Cosmetics Act, 21 U.S.C. §§ 301 *et seq.*, because it did not believe that market forces and the deterrent effect of tort law were sufficient to protect the public. Congress thus required the FDA to exercise its own independent judgment as to the actual safety and effectiveness of the drugs subject to its jurisdiction. It is not enough for the agency to ensure that drugs are produced in a context that one might *expect* to produce safe and effective drugs; the *actual* safety and effectiveness of the drug must be determined by the agency. This, even though drug companies must invest enormous amounts of money into the development of new drugs, and could argue that minimizing regulatory oversight by requiring the regulator to presume that market-produced drugs are safe and effective would lead to greater investment to the benefit of the general public.

So, too, in the context of utility regulation. In *FPC v. Texaco, Inc.*, 417 U.S. 380 (1974), the Court overturned a Commission order to the extent that it exempted small natural gas producers from the Act's rate-filing requirements. The Court explained that any presumption that "current contract prices in an area approximate closely . . . the just and reasonable rate. . . . would contradict the basic assumption that

has caused natural gas production to be subjected to regulation" in the first place. *Id.* at 398 (quoting *FPC v. Sunray DX Oil Co.*, 391 U.S. 9, 25 (1968)). "In subjecting producers to regulation because of anticompetitive conditions in the industry, Congress could not have assumed that 'just and reasonable' rates could conclusively be determined by reference to market price." *Id.* at 399.[3] *See also Wis. Gas Co. v. FERC*, 770 F.2d 1144, 1158 (D.C. Cir. 1985) (reliance on economic theory is no substitute for a reasoned exercise of the Commission's discretion).

To be sure, petitioners do not argue for a completely conclusive presumption. But a standard that permits alteration of contract rates only in extraordinary circumstances is no more consistent with congressional intent than one that regulates rates not at all. Congress did not enact the Federal Power Act to correct an occasional aberrant contract, leaving consumers in all other cases to pay the prices agreed to by utilities. Instead, Congress gave the Commission the responsibility to review utility rates

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[3] In *Morgan Stanley* the Court noted that while *Texaco* precludes the Commission from "implement[ing] a scheme of *total deregulation* by applying no standard of review at all to small producer rates," the decision said nothing to prevent the Commission from reviewing rates under the *Mobile-Sierra* doctrine. *Morgan Stanley Capital Group Inc. v. Pub. Util. Dist. No. 1 of Snohomish County, Wash.*, 128 S. Ct. 2733, 2746 (2008) (emphasis in original). We agree. Our point is simply that *Texaco*, and *Morgan Stanley*'s reaffirmation of it, precludes construing *Mobile-Sierra* in a way that effectively abdicates the Commission's regulatory responsibility, as petitioners would have the Court do here.

in order "to afford consumers a complete, permanent and effective bond of protection from excessive rates and charges." *Atl. Refining Co. v. Pub. Serv. Comm'n of N.Y.*, 360 U.S. 378, 388-89 (1959) (discussing Natural Gas Act). Congress believed that excesses were common in the natural gas and electricity industries and intended the Commission to exercise its powers vigorously in the protection of the public interest. *See, e.g., Sunray Mid-Continent Oil Co.*, 364 U.S. at 143; *NAACP v. FPC*, 520 F.2d 432, 438 (D.C. Cir. 1975). Petitioners' proposed presumption is fundamentally inconsistent with that intent.

2. Petitioners' plea for strict limits on the Commission's power to alter contract rates is particularly inappropriate given the lengths to which the Commission has already gone to relax regulatory review of market-based rates. Under its "market tariff system," the Commission has abandoned its obligation under Section 205, 16 U.S.C. § 824d, to review all rate changes before they are put into effect, instead permitting many sellers of wholesale power to file "market-based rate tariffs" that contain no rates but simply state that the utility intends to negotiate rates with purchasers in the future. *See Morgan Stanley Capital Group Inc. v. Pub. Util. Dist. No. 1 of Snohomish County, Wash.*, 128 S. Ct. 2733, 2741 (2008). At the same time, the Commission has precluded pre-implementation challenges under Section 205, 16 U.S.C. § 824d, under which the utility bears the burden of proving that the rate is just and reasonable. *See GWF Energy, LLC*, 97 FERC ¶ 61,297, at 62,391 (2001). Instead, the Commission will hear challenges to contract rates only under Section 206, where the challenger bears the burden of

proof and the Commission's power to order refunds is limited. *See* 16 U.S.C. § 824e(b); *see generally* Br. of Amici Curiae Col. Office of Consumer Counsel, *et. al.* at 13-20, *Morgan Stanley Capital Group, Inc. v. Pub. Util. Dist. No. 1 of Snohomish County, Wash.*, 128 S. Ct. 2733 (2008).

This Court has not passed on the legality of the Commission's market-based tariff regime, *see Morgan Stanley*, 128 S. Ct. at 2747, and has no occasion to do so here. But the Court should consider that the combined effect of the Commission's diminished review of rates and the presumption petitioners advocate would be the virtual elimination of any meaningful review for contract rates either before *or* after they are implemented, contrary to the manifest directives of the Act.

B. Congress Rejected The Premises Underlying Petitioners' Argument When It Enacted The Federal Power Act.

Petitioners' argument not only runs contrary to Congress's intent to subject wholesale electricity rates to significant regulatory review, but also is founded upon premises Congress rejected when it enacted the Federal Power Act. *See, e.g.*, *Texaco*, 417 U.S. at 399.

1. *In Enacting The Federal Power Act, Congress Rejected The View That Electricity Markets Can Be Counted On To Produce Rates Consistent With The Public Interest.*

At bottom, the arguments in favor of a presumption that contract rates are just and reasonable except in extraordinary circumstances are arguments against subjecting contract rates to regulatory oversight in the first place. Petitioners and their amici argue that contract rates should be presumed lawful in almost all circumstances because "contract rates negotiated by sophisticated parties can be expected to be reasonable even insofar as they affect third parties," Petr. Br. 35, as "the efficiency of private bargaining" leads "buyers and sellers . . . to negotiate contracts that maximize gains not only for themselves but also for society as a whole." Br. of Blaydon, *et al.* 10.

But Congress enacted public utility rate regulation because it disagreed with those assumptions.[4] Congress concluded that left unregulated, electricity market participants would not necessarily act in the interests of consumers and the broader economy. In *Sunray Mid-Continent Oil*, this Court explained that "the basic assumption that has caused natural gas production to be subjected to

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[4] The appropriate degree of government regulation of markets – be it markets for wholesale electricity, stocks, or mortgage-backed securities – is a topic of perennial debate among politicians and economists alike. *See* Paul Krugman, *How Did Economists Get It So Wrong?*, N.Y. TIMES, Sep. 6, 2009.

regulation" was that a utility "whose cost of purchase is a current operating expense which the [utility] is entitled to pass on its customers as part of its rates, lacks sufficient incentive to bargain prices down." 391 U.S. at 25-26. So, too, the Federal Power Act is premised on Congress's recognition that, for several reasons, the usual dynamics of supply and demand cannot discipline prices in the wholesale electricity market.

First, utilities generally can pass on the full cost of power purchases to their retail customers.[5] Because Congress gave the Commission exclusive authority over wholesale rates, the Supremacy Clause (implemented by the filed rate doctrine) requires that "a State may not exercise its undoubted jurisdiction over retail sales to prevent the wholesaler-as-seller from recovering the costs of paying the FERC-approved rate." *Nantahala Power & Light Co.* v. *Thornburg*, 476 U.S. 953, 970 (1986).

Second, utility purchasers often have a monopoly at the retail level, particularly in the market for service to residential customers. In such markets, there is little or no competitive pressure to keep retail prices low. *See, e.g.*, U.S. ENERGY INFORMATION ADMINISTRATION, THE CHANGING STRUCTURE OF THE ELECTRIC POWER INDUSTRY 2000: AN UPDATE 15, 41 (Oct. 2000) (explaining that retail service has historically been a monopoly and that only a few

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[5] By definition, wholesale electricity is purchased for *resale*. *See* 16 U.S.C. § 824(d).

states have begun to allow retail competition);[6] REPORT TO CONGRESS ON COMPETITION IN WHOLESALE AND RETAIL MARKETS FOR ELECTRIC ENERGY PURSUANT TO SECTION 1815 OF THE ENERGY POLICY ACT OF 2005 (as of 2006, 20 states and the District of Columbia allow retail competition but in most of them competition has been slow to develop, particularly for residential customers).[7]

Third, utilities do not necessarily increase their profits by negotiating lower wholesale prices. In many states, under a traditional "rate of return" regime, utility profits are regulated by a state commission, and lower wholesale costs may lead to lower retail prices, but not necessarily higher profits. *See, e.g.*, *Entergy La., Inc. v. La. Pub. Serv. Comm'n*, 539 U.S. 39, 42 (2003).

Fourth, many wholesale purchasers are unable to walk away from a deal simply because the price demanded is too high. A monopoly franchise for retail service brings with it a state law "obligation to serve" all customers who want electricity in the service territory. These utilities must procure enough power to provide reliable, adequate service to all those customers, regardless of wholesale prices. *See, e.g.*, Cal. Pub. Utils. Code § 451 (West 2009).[8]

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[6] Available at http://www.ferc.gov/legal/fed-sta/ene-pol-act/epact-final-rpt.pdf.

[7] Available at http://www.ferc.gov/legal/fed-sta/ene-pol-act/epact-final-rpt.pdf.

[8] Even in those states that have encouraged competition in the retail service sector, there is a designated "provider of last resort" that has a comparable obligation.

They do not have the option of reducing the level of service when costs soar, like commercial airlines do. Instead, these utilities have no option but to purchase whatever amount of electricity is required to meet their obligation to serve their customers, regardless of cost. *See Am. Gas. Ass'n v. FERC*, 912 F.2d 1496, 1516 (D.C. Cir. 1990) (wholesale sellers may extract monopoly profits because the retail provider must provide continuous service to its customers).

Fifth, transmission constraints limit the numbers of potential wholesale suppliers able to deliver power to specific "load pockets," or geographic areas where demand is high relative to available supply. *See, e.g., PJM Interconnection*, 121 FERC ¶61,173, at 61,790, n. 32 (2007). In such situations, competition among suppliers able to serve that load may be limited or nonexistent.

Sixth, it is not uncommon that wholesale purchasers will obtain power from affiliated companies, thereby reducing their incentive to bargain for the best prices. As the Commission has explained, when affiliated companies are "on both sides of the bargaining table," ensuring just and reasonable rates requires that the Commission "carefully scrutinize the rates, terms and conditions of the contract." *Ne. Utils. Serv. Co.*, 66 FERC ¶ 61,332, at 62,078 (1994); *see also S. Co. Servs., Inc.*, 67 FERC ¶ 61,219 (1994).

For these reasons, "neither the Commission nor [the courts] may merely assume, without analysis, that the [utilities'] protection of their own interests . . . will inure to the benefit of consumers" because "as regulated utilities, [they] might not have

a sufficient incentive, in dealing with [sellers], to minimize their costs." *Tejas Power Corp. v. FERC*, 908 F.2d 998, 1003 (D.C. Cir. 1990).

2. *Congress Did Not Believe That Active Regulatory Oversight Of Contract Rates Impedes Private Investment.*

Nor is there any reason to think that Congress accepted petitioners' assertion that the public interest demands that utilities generally be allowed to charge each other whatever rates they agree to (and ultimately to pass those costs on to their retail customers), because otherwise energy companies will refuse to invest in needed improvements to the nation's energy infrastructure. *See* Petr. Br. 39-41.

It is worth recalling that the nation's electric power infrastructure has been built by an industry operating within a highly regulated framework for over a hundred years. Since 1935, under the Federal Power Act, all wholesale contracts have been subject to review and modification by the Commission. During that time, there has been extensive infrastructure investment even though petitioners have not identified any case prior to 2002 in which the Commission applied the *Mobile-Sierra* presumption to a third-party challenge. *See* Petr. Br. 31-32 & n.7.[9] And although for the last few decades

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[9] This Court has made clear that even when *Mobile-Sierra* does not apply, the Commission must consider a utility's ability to attract capital and return on investment along with other factors. *See, e.g., Duquesne Light Co. v. Barasch*, 488 U.S. 299, 310 (1989).

the Commission has attempted to shift to a pro-market regulatory paradigm and away from traditional forms of regulation, that is a reason for confidence in, not skepticism about, the Commission's willingness to ensure that rate modifications will not unduly diminish market incentives for investment.

Petitioners and their amici present no evidence that without a guarantee of near inviolability for their contract rates, utilities will refuse to invest sufficiently in energy infrastructure improvements. Indeed, in this very case, petitioners agreed that challenges to rates brought within 45 days of the capacity auction would be reviewed by the Commission without any *Mobile-Sierra* presumption. *See* J.A. 118-19; Pet. App. 78a, 120a. And many other utilities voluntarily subject their contract rates to "ordinary" just and reasonable review through so-called "Memphis clauses." *See, e.g.*, *United Gas Pipe Line Co. v. Memphis Light, Gas, and Water Div.*, 358 U.S. 103, 113-14 (1958).

The Federal Power Act affords substantial protection of contract stability without the need to impose petitioners' generally insurmountable presumption. For one thing, the Act provides a mechanism for early challenges to rates through pre-implementation challenges under Section 205, 16 U.S.C. § 824d. This process allows the Commission to consider the lawfulness of a rate before parties to the contract have invested heavily in reliance on the proposed rate. To be sure, the Commission has rendered that protection largely ineffective by refusing to consider Section 205 challenges to market-based rates, but that is a reason to declare that practice unlawful, not to justify yet further

departures from the regulatory scheme Congress enacted. Moreover, once rates have gone into effect, Section 206, 16 U.S.C. § 824e, promotes contract stability by placing a "heavy burden" on any challenger to show that a rate is unjust and unreasonable. *Hope Natural Gas Co.*, 320 U.S. at 602. And, as discussed next, Congress has given the Commission ample authority to deny requests for rate changes when doing to would unduly undermine contract stability in conflict with the public's interest in encouraging long-term investment to ensure a stable supply of electricity.

C. Congress Delegated To The Commission, Not The Courts, The Responsibility To Decide How Much Weight To Give The Fact That A Rate Was Set By Contract.

Imposing greater restraint on the Commission's exercise of discretion also would be fundamentally inconsistent with the Act's allocation of power and responsibility between the Commission and the courts.

1. Congress has entrusted the regulation of wholesale electricity prices to the informed judgment of the Commission, not to the reviewing courts. *Mont.-Dakota Utils. Co. v. Nw. Pub. Serv. Co.*, 341 U.S. 246, 251 (1951); *see also In re Permian Basin Area Rate Cases*, 390 U.S. 747, 767 (1968). For that reason, this Court has repeatedly emphasized that the Commission is "not bound to the use of any single formula or combination of formulae in determining rates," but rather has broad discretion to determine for itself what factors are relevant and how much

weight each should be given. *Hope Natural Gas Co.*, 320 U.S. at 602 (citing *Natural Gas Pipeline Co. of Am.*, 315 U.S. 575, 586 (1942)); *see also Mont.-Dakota Utils. Co.*, 341 U.S. at 251 ("Statutory reasonableness is an abstract quality represented by an area rather than a pinpoint. It allows a substantial spread between what is unreasonable because too low and what is unreasonable because too high.").

Congress delegated to the Commission principal responsibility for reconciling the competing interests in ensuring both reasonable rates and adequate investment because the question requires expertise regarding exceedingly complicated and ever changing markets. *See, e.g.*, *Permian Basin*, 390 U.S. at 767. Here, petitioners have provided the Court no reason to think that Commission error is so inevitable that its discretion must be subject to the extraordinary discipline of a strong court-imposed presumption. To the contrary, in exercising its statutory authority to modify contracts, the Commission has not modified contracts lightly (and petitioners do not claim that the Commission has abused its discretion). In addition, petitioners' presumption would make a single factor (the existence of a contract), the nearly conclusive consideration in what ought to be a far more encompassing, and far less constrained, inquiry. *See, e.g.*, *Tejas*, 908 F.2d at 1003 (Commission accords "some weight" to the fact of a contract, but must exercise its independent judgment and consider other relevant factors).

2. This does not mean, however, that the Court should defer to the Commission's inexplicable acquiescence in petitioners' attempts to diminish its authority. While the Commission's special expertise

in utility regulation commands deference to its views on whether a particular rate is just and reasonable, that expertise has no bearing on the question of whether this Court's decisions in *Mobile*, *Sierra*, and *Morgan Stanley* extend to third-party challenges. *See* FERC Br. 17-22 (basing position on its construction of those decisions); *Ledbetter v. Goodyear Tire & Rubber Co., Inc.*, 550 U.S. 618, 642 n.11 (2007) ("Agencies have no special claim to deference in their interpretation of our decisions."). Moreover, as petitioners concede, the Commission's current position is of recent vintage and conflicts with the view it took prior to 2002 that *Mobile-Sierra* did not apply to third-party challenges. *See* Petr. Br. 32 n.7; *see also* Resps. Br. 32 & n.3 (collecting Commission opinions to that effect). The lack of consistency also diminishes any deference its interpretation would otherwise be due. *See, e.g., United States v. Mead Corp.*, 533 U.S. 218, 228 (2001).

D. Any Further Restraints On The Commission's Authority Must Come From Congress.

If further constraints on the Commission's discretion are warranted in light of changes in energy technology and markets, *see generally Morgan Stanley*, 128 S. Ct. at 2740-41, they should come from Congress, not from a decision of this Court. "It may be, as some economists have persuasively argued, that the assumptions of the 1930's . . . if true then, are no longer true today." *Texaco*, 417 U.S. at 400. But responsibility for revising the Act in light of those changes lies with Congress. *Id.* ("It is not the Court's role, however, to overturn congressional

assumptions embedded into the framework of regulation established by the Act."); *see also New York v. FERC*, 535 U.S. 1, 24 (2002).

It is therefore notable that in 2005, Congress rejected a proposal that would have provided that the Commission "shall have no authority to abrogate or modify any provision of an executed contract . . . that has been entered into or taken effect, except upon a finding that failure to take such action would be contrary to the public interest." H.R. 6, 109th Cong. § 1286(a) (as passed by House, Apr. 21, 2005). This language would have extended the holding of *Mobile* and *Sierra* to third-party contract challenges, but would not have included the strong presumption of lawfulness petitioners seek. And even that more modest extension of the *Mobile-Sierra* doctrine to third-party challenges failed to pass. Whatever else may be read into that rejection, it demonstrates that the doors of Congress are open to those who would argue that the nation's approach to regulation of electricity service requires fundamental revision.

III. At The Very Least, No Presumption Should Apply When Contract Rates Are Challenged By State Public Utility Commissions Or The Federal Commission Itself.

Even if the Court concludes that contract rates ordinarily should be presumed just and reasonable in third-party challenges, the Court should not extend the presumption to challenges by state public utilities commissions or to investigations initiated by the Commission *sua sponte*.

1. As instrumentalities of co-equal sovereigns in an area subject to joint state and federal regulation,

the views of a state commission are entitled to a level of respect entirely unlike that owed to private citizens, interest groups, and corporations. *See Ark. Elec. Coop. Corp. v. Ark. Pub. Serv. Comm'n*, 461 U.S. 375, 377 (1983) (recognizing that the "regulation of utilities is one of the most important of the functions traditionally associated with the police power of the States"). State commissions bring to bear unique substantive expertise in the regulation of public utilities. Indeed, state commissions have been regulating electrical utilities for the public interest longer than the federal government. *See, e.g., New York v. FERC*, 535 U.S. at 5-6. And they are charged, no less than the Commission, with the responsibility "to insure the public adequate service at reasonable rates without discrimination." *Pac. Tel. & Tel. Co. v. Pub. Util. Comm'n*, 62 Cal.2d 634, 647 (1965).

In this way, state commissions differ from other third parties who may focus principally on reducing short-term rates. Like the Commission itself, state commissions must attend to the important interests of contract stability, the economic well-being of utilities, and the maintenance of incentives for long-term investment. *Cf. Los Angeles v. Pub. Util. Comm'n*, 15 Cal.3d 680, 694 (1975) (noting the duty of the Public Utilities Commission of the State of California to consider "every element of public interest affected by" the operation of public utilities).

As a consequence, federal law grants state commissions special status in proceedings to determine whether wholesale rates are consistent with the public interest. Congress enacted Title II of the Federal Power Act to "supplement" state regulation, to "aid the State commissions in their

efforts to ascertain and fix reasonable charges," and to "assist the States in the exercise of their regulatory powers." *Conn. Light & Power Co. v. FPC*, 324 U.S. 515, 525-26 (1945).[10] The new provisions were "in no sense a usurpation of State regulatory authority and contain throughout directions to the Federal Power Commission to receive and consider the views of State Commissions." *Id.* at 526. State commissions thus have long played a critical role before the Commission in cases where the justness and reasonableness of wholesale electric rates is adjudicated. In fact, the Act specifically identifies state commissions as among those the Commission may allow to intervene as parties in federal rate proceedings 16 U.S.C. § 825g(a).[11] *See also id.* § 825*l* (same with respect to identifying parties entitled to petition for rehearing of Commission decisions); *Md. People's Counsel v. FERC*, 760 F.2d 318, 320-21 (D.C. Cir. 1985) (Scalia, J.) (noting that similar provisions of the Natural Gas Act "reflected" Congress's "special solicitude for states and state agencies . . . in protecting their citizens in this traditional governmental field of utility regulation").

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[10] The Act also declares that its provision shall "extend only to those matters which are not subject to regulation by the States," 16 U.S.C. § 824(a), and specifically preserves the authority of "a State or State commission" in certain traditional areas, including the retail sale of electricity. *Id.* § 824(b)(1).

[11] The Commission has likewise recognized the special status of state commissions by allowing them to intervene as a matter of right in Commission proceedings. 18 C.F.R. § 385.214(a)(2).

This Court has held that the Commission's similar combination of expertise and legal responsibilities warrant giving its views on the lawfulness of rates great deference. *See Texaco*, 417 U.S. at 389; *see also FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 602 (1944) (Commission orders are "the product of expert judgment which carries a presumption of validity"). The views of the Commission's state counterparts are due deference for the same reason. When a state commission challenges a particular rate as inconsistent with the public interest, the deference owed to that expert view should more than overcome any general presumption that private contract negotiations produce just and reasonable rates consistent with the public interest.

2. For similar reasons, the Commission should be free of the burden of any presumption when it initiates an investigation of rates *sua sponte*, based on its informed view that they may conflict with the public interest.

While this Court has described the *Mobile-Sierra* presumption as a limitation on the powers of the Commission to set aside contract rates at the request of a party, it has done so in the context of cases in which the Commission itself had seen no reason to instigate an investigation on its own. When the Commission has seen no basis to doubt the lawfulness of a rate of its own accord, and when no third party representing the public interest has complained, there may be good reason to be reluctant to overturn a contract rate simply because a party to the contract would prefer a more profitable rate. But when the Commission itself takes the unusual step of

initiating a rate investigation, given the deference owed to the Commission's rate expertise, no presumption should constrain the Commission's exercise of its most basic statutory duties.

IV. Whether The Commission Could Lawfully Choose To Adopt A Stricter Standard Of Review Of Its Own Volition Is Not Before The Court.

This Court granted certiorari to decide a limited question: "Whether *Mobile-Sierra*'s public interest standard applies when a contract rate is challenged by an entity that was not a party to the contract." Petr. Br. i. For the reasons set forth above, and in the brief for respondents, the answer to that question is "no." Nothing in *Mobile*, *Sierra*, or this Court's other cases requires the Commission to presume that a contract rate challenged by a third party is just and reasonable, absent extraordinary circumstances.

The Commission agrees that it is not required by this Court's cases to apply the *Mobile-Sierra* presumption to the rate challenges at issue in this case, albeit for different reasons that those presented in this brief. *See* FERC Br. 28-32. But it nonetheless asserts that the decision below should be reversed on an alternative ground. It argues that even if it was not *required* to apply the *Mobile-Sierra* public interest standard as provided in the settlement agreement it approved, it nonetheless lawfully adopted that standard as a matter of discretion. FERC Br. 28-32. This Court should not decide that question in this case.

First, if the Commission intended to ask the Court to pass on the scope of its authority to impose a

Mobile-Sierra standard as a matter of discretion, it was required to seek certiorari on that question. *See* S. Ct. R. 14.1(a) ("Only the questions set out in the petition, or fairly included therein, will be considered by the Court."). But the Commission did not even hint at its present theory in its certiorari-stage brief. In fact, not only did the Commission decline to seek certiorari on the question it now asks the Court to decide, it affirmatively opposed plenary review of the decision below. FERC BIO 8.

Second, it does not appear that the court of appeals understood the Commission to be making the argument it now presses, or that the Commission made clear below the distinction it now draws between circumstances in which it is *required* to apply the *Mobile-Sierra* standard and the occasions on which it has discretion to adopt it. *See* Pet. App. 19a-24a; FERC CA Br. 53-58. This Court should not decide such an important and complicated question without the benefit of a lower court decision that squarely addresses it on the basis of adequate briefing from the Commission and the parties.

Third, there is no reason to think that affirming without considering the Commission's new argument will unduly prejudice the parties. There is no way to know whether anyone will ever challenge the results of the capacity auctions pursuant to the settlement. Nor is there any reason to assume that the difference in the standard of review would make a difference to any such challenge. *See* FERC BIO 10-12. Indeed, affirming here will not predetermine the weight the Commission may afford the public's interest in contract stability and greater investment in the New England capacity market in any future challenge.

See FERC BIO 10-12. And the Commission has made clear by its brief in this Court that it takes those interests very seriously, a position that should give investors substantial confidence that the rates established under the settlement will not lightly be modified.[12]

That said, if the Court were to excuse the Commission's waiver of its alternative grounds for reversal and accepted its position, the Court should resolve the case on that ground and leave for another day the broader question of whether *Mobile-Sierra* applies of its own force to all challenges to all bilateral contracts.

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[12] Even while insisting that the Question Presented is irrelevant to the proper disposition of this case – because, it says, this case does not involve the kind of contract to which the *Mobile-Sierra* presumption applies, *see* FERC Br. 28-32 – the Commission nonetheless claims that the Court should reverse the court of appeals for giving the wrong answer to that irrelevant question. FERC Br. 22. But if the Question Presented does not arise on the facts of this case, the proper resolution would be to dismiss the petition as improvidently granted or to affirm the decision below on the ground, supported by the Commission, that the court of appeals was right in concluding that the *Mobile-Sierra* doctrine does not apply.

CONCLUSION

For the foregoing reasons, the judgment of the court of appeals should be affirmed.

Respectfully submitted,

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